



BULGARIAN
DEVELOPMENT BANK

Annual Report

2018



<http://www.bbr.bg/>



BULGARIAN
DEVELOPMENT BANK

Annual Report

BULGARIAN DEVELOPMENT BANK GROUP



**Consolidated
Annual Management Report**



Independent Auditors' Report



**Consolidated Annual Financial
Statement**

2019

General information

BULGARIAN DEVELOPMENT BANK AD

Shareholding structure as at 31 December 2018

The State through the Minister of Economy – **99.9999%**
and DSK Bank – **0.0001%**.

Supervisory Board:

Luchezar Borisov – *Chairman of the Supervisory Board;*
Mitko Simeonov – *Vice Chairman of the Supervisory Board;*
Velina Burska – *Member of the Supervisory Board.*

Management Board:

Stoyan Mavrodiev – *Chairman of the Management Board and Chief Executive Director;*
Rumen Mitrov – *Vice Chairman of the Management Board and Executive Director;*
Nikolay Dimitrov – *Member of the Management Board and Executive Director.*

Head office and registered address:

1000 Sofia, Sredets area, 1 Dyakon Ignatii Street
Registration Number – **UIC 121856059**

Join auditors of Bulgarian Development Bank AD:

Ernst & Young Audit OOD
Polygraphia Office Centre
47A Tsarigradsko Shose Blvd., floor 4
Sofia 1124
office.sofia@bg.ey.com

Zaharinoва Nexia OOD
157-159 Konstantin Velichkov Boulevard
Floor 1, Office 3
Sofia 1309
office@zaharinovanexia.com

Auditor of National Guarantee Fund EAD and Micro Financing Institution Jobs EAD:

Ernst & Young Audit OOD
Polygraphia Office Centre
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Sofia 1124
office.sofia@bg.ey.com

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Address to the Shareholders

Dear Shareholders,

The Bulgarian Development Bank Group is dedicated to its mission of encouraging entrepreneurship, boosting the economic, export and technological potential of SME.s, and achieving the targets, principles and priorities entrusted to us by the legislator and integrated in our strategy, in turn approved by the Government.

In 2018, we marked the 10th anniversary of the adoption of the BDB Act. This important legislation, transformed the Encouragement bank into the Bulgarian Development Bank thereby laying the foundation of a fully-fledged banking group, capable of lending support of scale to economic development, the convergence priorities and the financial and economic integration of Bulgaria to the other EU economies.

In line with our mandate under the BDB Act, in 2018 we set up the Capital Investment Fund – a wholly owned subsidiary with registered capital of BGN 65 million. The Fund shall provide equity to small and medium sized enterprises and start-ups, with the objective to improve their business competitiveness, support their research and development activities, scale their production capacity, support EU funds absorption and provide financial backing at the early stages of development, before they are able to access (regulated) capital and loan markets. During the year, we prepared the start and registration of the subsidiaries BDB Leasing and BDB Factoring, subsidiaries that shall be operational in 2019. Together with the National Guarantee Fund, the Microfinance Institution Jobs and the Capital Investment Fund, BDB grew to a fully-fledged financial group, prepared to address the needs of Bulgarian businesses and entrepreneurs, as well as comprehensively support our clients. growth plans.

2018 was a record year for both the banking sector in Bulgaria and the activities of the BDB Group. The assets of the Bank reached BGN 3 billion, growing by 22% y-o-y. We extended BGN 400 million in new loans, a more than fourfold increase compared to 2017. We increased the number of companies supported through our on-lending programs. Our National Guarantee Fund increased its portfolio of guarantees by 30% and the volume of guarantees issued by 24% y-o-y. During 2018, the BDB Group funded directly and indirectly 2 495 end-customers, 99% of which small and medium-sized enterprises.

The 2018 operating income of BDB Group before impairments and provisions amounted to BGN 64 562 thousand, while the net profit amounted to BGN 27 087 thousand and the net expenses for impairments and provisions stood at BGN 10 046 thousand during that year.

Building on the identity, credibility and international activity of our banking group, in pursuit of our mandate for attracting and managing funds and projects with international financial and other institutions, in 2018 we concluded a framework agreement with the Chinese Development Bank for EUR 1.5 billion, exceeding the total internationally raised funding in the 20-year history of the Bank. BDB is proving to be the best positioned bank to raise funds from international financial institutions and partners and, as at December 2018, is a party to 13 funding agreements with 8 international financial institutions.

At the same time BDB observed strict market discipline and acted in full compliance with the macro-prudential rules and supervisory standards, as per the requirements of European and national banking regulations. The Bank maintained the highest levels of liquidity and capital adequacy in the Bulgarian banking system.

In addition to the core activities of the BDB Group, in 2018 we took the lead in fostering talks with our national development bank peers and partners in the region to contribute and increase our regional and European cooperation with the ultimate goal to accelerate sustainable economic growth, infrastructure development and trade connections between our economies.

In April 2018, under the Bulgarian Presidency of the Council of the European Union, BDB launched an international annual forum under the slogan “Infrastructure for Growth” attended by European, multilateral and national development banks. The discussions highlighted the priorities and potential for enhancing the role of promotional financial institutions in fostering economic and infrastructural cohesion in Southeastern Europe and the Balkans in particular. The BDB Forum ended with the adoption of a Memorandum of Cooperation between six national and multilateral banks: BDB, the Croatian, Hungarian and Macedonian Development Banks, the Black Sea Trade and Development Bank and the International Investment Bank. This platform is open to new partner institutions and aims to promote large-scale regional development projects and programs without accumulating debt by national governments but through mobilizing alternative resources.

In July 2018, BDB hosted the first international meeting of the Interbank Association of China and the Countries of Central and Eastern Europe. A Cooperation Program for the period 2018 – 2020 was signed as well as an agreement on capacity building and know-how sharing. These are the Association’s first official documents since its establishment in November 2017 in Budapest. The meetings of the Interbank Association preceded the 7th Annual Meeting of the Heads of State and Government of the countries of Central and Eastern Europe and China under the 16 + 1 mechanism hosted by the Republic of Bulgaria. In the presence of the Prime Minister of Bulgaria Mr. Boyko Borisov and the Prime Minister of China Mr. Li Keqiang, together with the Chairman of the Management Board of the China Development Bank Mr. Hu Huaibang, we concluded a framework agreement for EUR 1.5 billion between our two development banks

We entered 2019 with the highest financial results, capital base and credit rating in our 20-year history. Building on the established international confidence in the BDB Group, confirmed with the agreements signed in 2018, we currently have a stable resource base in order to fulfil our mission, expand the Bank’s role in supporting entrepreneurship and growth of Bulgarian businesses and their expansion in the region, the EU and globally.

We assembled and trained an excellent team of professionals to confront future challenges, help our clients finance their business, as well as support the government in funding strategic priorities in infrastructure and economic development, and countering changes in the global cycle of economic activity and trade. BDB enters its third decade as a banking institution and group capable of delivering complex and innovative high-value-added solutions to our customers, the market in general and our shareholders.

I would like to thank the management and all employees for these achievements, their commitment and tangible contribution to our success. I would also like to thank our customers, partner organizations and shareholders for their continued trust in the Bank and the Group.



STOYAN MAVRODIEV

Chairman of the Management Board

Chief Executive Officer

**Consolidated
Annual Management
Report**

31 December, 2018

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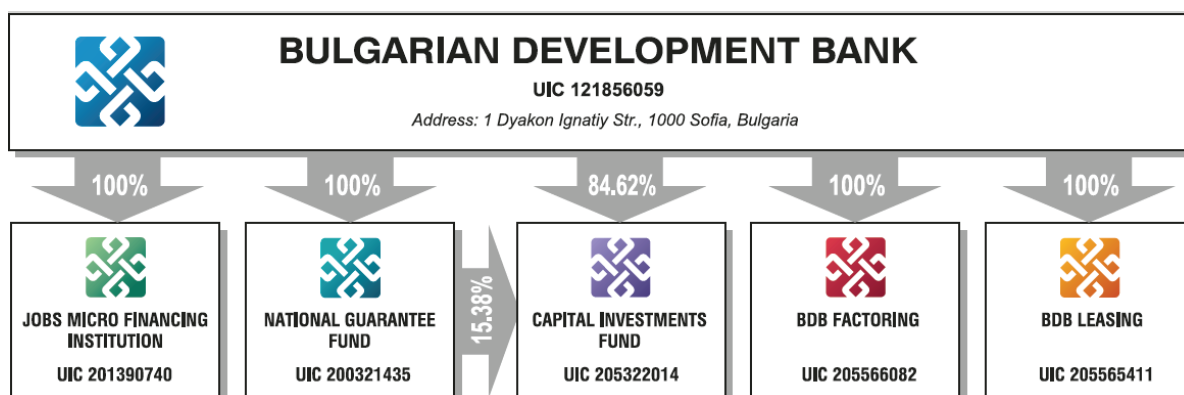


Information about the BDB group

The BDB group

At the end of 2018, the Financial Group Bulgarian Development Bank (the „Group“¹, or the Financial Group) comprises the Bulgarian Development Bank AD („BDB“, the „Bank“) and its subsidiaries – the National Guarantee Fund EAD (NGF), the Micro Financing Institution Jobs EAD (MFI Jobs) and the Capital Investments Fund AD (CIF).

At the beginning of 2019, the Bank incorporated two new subsidiaries – BDB Leasing EAD and BDB Factoring EAD, which will become members of the Financial Group of BDB as well. At the date of preparation of the Report, the structure of the BDB Financial Group is presented in the following table:



The average number of staff as at 31 December 2018 of the BDB Group was 210 (as at 31 December 2017: 197).

At the end of 2018, the BDB Group had no liabilities under existing or new issues of securities.

As of 31 December 2018, there were no pending court, administrative or arbitration proceedings related to liabilities or receivables of the BDB Group, amounting to 10 per cent or more of its equity.

The BDB Group complies with the applicable Bulgarian and European environmental protection legislation. The Bank conducts an environmental impact analysis of all projects for which such an analysis is required under the applicable legal framework. In the project implementation process, the BDB Group requires the submission of the necessary permits and documents, and strictly monitors the precise implementation of the projects. Subject to stricter environmental requirements set out in the loan agreements with external creditors, BDB requires compliance with these higher standards by its clients and monitors their performance.

In the field of human resource development, the BDB Group focuses on continuing support for development and training of staff, creating prerequisites for professional growth of their highly qualified professionals.

The BDB Group has no dedicated R&D unit and is currently not planning activities in this area, except for staff trainings.

The Group's financial performance and ratios are stable. There are no non-financial indicators, the value of which would affect the results of its principal activity.

¹ At the end of 2018, the Bank was a sole owner of the capital of TP Maritsa EOOD (TPM); however, the company was not a part of the strategic business model of the Financial Group of BDB.

Bulgarian Development Bank AD

The Bulgarian Development Bank AD was established on 11 March 1999 as a joint-stock company under the name of Encouragement Bank AD. By means of the Bulgarian Development Bank Act (BDBA), on 23 April 2008 the name and scope of activity of the Bank were changed, so as to be able to apply schemes and instruments to finance public investments and projects of priority for the country's economy.

Being the only state-owned bank in the country, BDB provides funding for programmes specifically entrusted to it specifically by the government of the Republic of Bulgaria. The exposure to a customer or group of related clients, other than credit institutions, central governments and central banks, complies with the requirements and limits of Regulation 575/2013/EU taking into account the effect of credit risk mitigation under a procedure laid down by the Management Board.

Bulgarian Development Bank AD holds a license for an investment intermediary according to which it may provide investment services and perform investment activities² under Article 6, paragraph 2 of the Markets in Financial Instruments Act (MFIsA), as well as additional services under Art. 6, paragraph 3 of the MFIsA.

The Bank does not provide investment services, or perform investment activities under Article 6, paragraph 2, items 8 and 9 of the MFIsA – organisation of a multilateral trading facility and an organised trading facility.

As of 31 December 2018, the paid-in capital was BGN 601,774 thousand (31 December 2017: BGN 601,774 thousand). The capital consists of 6,017,735 ordinary registered voting shares of par value BGN 100. As of the date of preparation of this report, the ownership of the capital is distributed as follows: 99.9999% of it is held by the Republic of Bulgaria, represented by the Ministry of the Economy, 0.0001% is held by DSK Bank.

BDB is governed in accordance with Article 5 of BDBA, according to which the Bank has a two-tier management system with the Minister of Economy exercising the state's rights at the General Assembly of Shareholders of the Bank. Members of the BDB's management bodies are appointed in compliance with BDBA, Credit Institutions Act, Commercial Act, and the Regulations on their implementation, adopted by Bulgarian National Bank.

Bulgarian Development Bank AD has not acquired treasury shares pursuant to Article 187e.

BDB is not a party to transactions falling within the scope of Article 240b of the Commercial Act with reference to Article 247 of the same Act.

There are no shares of the entity acquired, held or assigned during the reporting year by the members of the management bodies. Pursuant to Article 6, paragraph 4 of the BDBA, the members of the Management and controlling bodies, the procurators and the senior management cannot hold shares and cannot be provided with options for shares of BDB, and in subsequent accounting periods no agreements may be concluded as a result of which in any future period changes may occur the relative volume of shares held by current shareholders.

The average number of staff at the end of 2018 was 191.

Bulgarian Development Bank AD has no branches. The head office and registered address of BDB is at 1 Dya-kon Ignatii Street, Sofia City.

² Investment services are provided and investment activities are performed in accordance with the requirements of MFIsA, Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (Directive 2014/65/EU or MIFID II), Regulation (EU) 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012 (Regulation (EU) 600/2014), Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive (Delegated Regulation (EU) 2017/565) and the acts on their implementation.

National Guarantee Fund EAD (NGF)

- National Guarantee Fund EAD (NGF) is a company founded on 12 August 2008 on the basis of the Bulgarian Development Bank Act (BDBA) and was registered at the Commercial Registry on 22 August 2008. National Guarantee Fund EAD is a financial institution, registered in 2009 by the BNB in the Register under Article 3, Paragraph 2 of the Credit Institutions Act (LCI). In accordance with the Articles of Association of the company, the subject of acssuing guarantees for supplementing the collateral under loans to small and medium-sized enterprises;
- Offering other products to small and medium-sized enterprises, like: guarantee for participation in a tender; performance guarantee; advance payment guarantee; guarantee for payment of a loan of an exporter, etc;
- Issuing guarantees for supplementing collateral under loans to small and medium-sized enterprises, carrying out research and development and for implementing these products and scientific developments into the industry;
- Other activities, not particularly prohibited by law.

The registered capital of the company as of 31 December 2018 amounted to BGN 80,000,000 split into 800,000 shares with nominal amount of BGN 100 each, the shares are ordinary, materialised, registered and indivisible, and each share give the right to one vote. The company.s capital is fully paid-in.

The seat and registered address of the National Guarantee Fund EAD (NGF) is Sofia, 1 Dyakon Ignatii St.

The average number of staff of NGF at the end of 2018 was 8.

As of 31 December 2018, National Guarantee Fund EAD had no branches.

Micro Financing Institution Jobs EAD (MFI Jobs)

Micro Financing Institution JOBS EAD (MFI Jobs) was registered into the Commercial Registry on 14 January 2011. The scope of activity is micro-financing, including providing micro-loans, acquiring from third parties and leasing industrial equipment, automobiles and other vehicles, as well as other items /finance lease/, purchase and sale, and import of such items, consulting services, trade representation and mediation for local and foreign physical and legal bodies performing their activity in the country, as well as any other activity not forbidden by law.

The registered capital of MFI Jobs as of 31 December 2018 amounted to BGN 7,643,000 split into 76,430 shares with nominal amount of BGN 100 each, the shares are ordinary, materialised, registered and indivisible, and each share give the right to one vote. The company.s capital is fully paid-in.

The seat and registered address of Micro Financing Institution Jobs EAD is Sofia, 1 Dyakon Ignatii Str.

The average number of staff of NGF at the end of 2018 was 11.

As of 31 December 2018, Micro Financing Institution Jobs EAD had no registered branches.

Capital Investments Fund AD (CIF)

Capital Investments Fund (CIF) was incorporated on 24 August 2018 and registered on 04 October 2018 as a joint-stock company with 100 percent of ultimate participation of BDB (84.62% of direct participation of BDB, or 550,000 shares, and indirect participation through NGF – 15.38%, the owner of the remaining 100,000 shares). The registered address of MFI is at 1 Dyakon Ignatii St., Sofia. The registered capital of as of 31 December 2018 consisted of 650,000 registered shares with nominal amount of BGN 100, including paid-in capital as of 31 December 2018 of BGN 16,250,000.



- The scope of activity of CIF include Participation in the capital of small and medium-sized enterprises;
- Provision of consulting services regarding the capital structure of small and medium-sized enterprises; advice and services on incorporation of entities under Article 261 of the Commercial Act;
- Investment consultancy;
- Consulting services on the management of pools of securities of small and medium-sized enterprises;
- Other activities, not specifically prohibited by law.

As of 31 December 2018, CIF had no registered branches; it did not carry out operating activities and therefore, the Fund had no employees neither had it generated income.

Main focus activities and projects in 2018

Key events

In line with the 2017-2020 Strategy, efforts at the BDB Group during the year were aimed at increasing the share of indirect financing (including the volume of loans with guarantees issued by NGF).

In 2018, Bulgarian Development Bank established Capital Investments Fund, and the process on incorporating two new subsidiaries — BDB Leasing and BDB Factoring, began. These two, newly incorporated entities, together with National Guarantee Fund, Micro Financing Institution Jobs and Capital Investments Fund supplement the BDB Group providing new opportunities for providing the Bulgarian businesses with financing.

In 2018, the Bank prepared itself for the implementation of the new requirements of MFISA, Directive 2014/65/EU, Regulation 600/2014, Regulation 2016/679 on the protection of personal data (GDPR), the new Payment Services and Payment Systems Act (PSPSA), and Ordinance NO. 3 on payments of BNB and Directive 2015/2366 (PSD 2) on payment services, so that they are successfully implemented in 2018. The Bank has established and is applying organization related to the execution and performance of contracts with customers, to the client information requirement, to record keeping and safekeeping of client assets, pursuant to the requirements of the above mentioned national and European legislation. The Bank has built a system of internal rules and procedures for internal control, which ensure full compliance with the legal provisions specified above.

In 2018, the main IT activities were focused in two directions – in implementation of regulatory projects, improvement of the day-to-day operational IT activities, and updating the working procedures. The most significant projects were as follows: preparation of the bank and making its information systems compliant with GDPR requirements; fulfilment of reporting requirements and enrichment of the system.s functionalities in accordance with the requirements of MIFID II, preparation for and implementation of the latest SWIFT standards, and preparation for full comprehensive outsourcing of the SWIFT service to BORIKA aiming at improving its reliability, as also in line with the latest SWIFT security requirements. A modern anti money laundering system was selected in accordance with the most recent regulatory requirements and the bank started preparing itself for the launch of the implementation project in 2019.

In 2018, the international rating agency Fitch Ratings carried out its regular annual review and confirmed the credit rating of the Bulgarian Development Bank AD. **In April 2019, Fitch Ratings Agency upgraded the outlook of the long-term credit rating of BDB from BBB Stable Outlook to BBB, Positive Outlook.** This is the highest credit rating assigned to a Bulgarian financial institution, and for BDB it is limited by the rating of the sovereign – the Bulgarian State.

Rating effective as of	As of 31 December 2017	As of 31 December 2018	As of the date of preparation of the Management Report
Date of preparation of the rating:	13.12.2017	06.12.2018	20.04.2019
Long-term Rating (IDR, SRF)	„BBB“	„BBB“	„BBB“
Outlook	Stable	Stable	Positive

The rating agency's assessment is based on the reliable support of the sovereign – the Bulgarian State, the BDB's good financial performance, its good capitalisation, and its role in supporting the government's economic policy. The positive outlook shows the existence of a balance in risks associated with credit rating assessments. The agency's notification states that, in the event of a subsequent increase in Bulgaria's rating, the BDB's rating will most likely be increased.

The stable equity base contributes significantly to the high capital adequacy. BDB is the institution with the highest level of capitalization in the banking system of Bulgaria, significantly above the regulatory minimum.

The General Assembly of Shareholders of BDB held in July 2018 approved the audited financial statements of the institution for 2017, certified by the joint auditors, Ernst & Young Audit OOD and Zaharinoва and Partners OOD (the latter company with a current name Zaharinoва Nexia OOD). Bulgarian Development Bank reported a profit for distribution for 2017 amounting to BGN 8,858 thousand (after considering the effect of the application of IFRS 9). The General Assembly took a decision to distribute the 2017 profit of the Bank as follows:

- contributions to the Reserve Fund amounting to 10 percent, or BGN 885 thousand;
- the remaining balance of the profit of Bulgarian Development Bank AD for 2017, net of contributions to the Reserve Fund, to be taken to Additional Reserves heading. Following this resolution, the capital adequacy of Bulgarian Development Bank continues to be the highest one in the Bulgarian banking system.

In 2018, the **product and credit portfolio of the Bank continued to develop**, as also the diversification of the sources of financing.

In May 2018, the last amount on the principal of the loan with the Japan Bank for International Cooperation was repaid and thus, the loan was fully repaid.

BDB was the first President by rotation and took the host's role at the First International Meeting of the China-CEEC Interbank Association of China and the Central and Eastern European countries.

In the framework of the meeting, at the beginning of July 2018, on a bilateral basis, BDB and the Chinese Development Bank (CDB), **as part of the official agenda of the Seventh Annual Meeting of China's and CEE's Heads of Government, signed a financial cooperation agreement under the One Road, One Belt initiative. The agreement envisages a financing of EUR 1,500 million for the upcoming 5 years**, as follows:

- Up to one billion Euro will be allocated for joint financing, project financing, joint equity investment funds, syndicated loans and other projects of mutual interest agreed between BDB and CDB within the One Road, One Belt initiative.
- At least EUR 500 million will be the amount of bilateral co-financing for BDB, which will be available for projects under the One Road, One Belt initiative and / or in accordance with the BDB's strategy; these projects may include, but are not limited to: support to SMEs, energy, communication, transport, agriculture in Bulgaria, or for other purposes as might be approved by BDB.
- The total amount under the agreement is 75% of the financial initiative of the Chinese Development Bank within the China-CEEC Interbank Association of China and the Central and Eastern European countries of EUR 2 billion.
- On the grounds of the financial cooperation agreement under the One Road, One Belt initiative, on 13 December 2018 BDB signed a third Loan contract with the Chinese Development Bank EUR 300 million and a 10-year term; the purpose of the loan is to support the Bulgarian business. The first tranche of the new loan of EUR 30 million was utilised as of 31 December 2018.

In August 2018, the loan from Industrial and Commercial Bank of China was fully repaid in accordance with the repayment schedule.

In 2018, the entire agreed amount EUR 50 million under the agreement signed on 28 September 2017 with the Chinese Exim Bank was utilised.

A financing contract amounting to EUR 5,745 thousand was signed with a Bulgarian commercial bank for the purpose of promoting micro-, small- and medium-sized enterprises. BDB is a borrower under a Loan contract with the Government of the Republic of Bulgaria. The contract was signed on the grounds of a Treaty between the Government of the Federal Republic of Germany and the Government of the Republic of Bulgaria for financial cooperation.

Bulgarian Development Bank concluded the first contract for on-lending financing with a commercial bank within the framework of the Investment Plan for Europe. The funds under the programme have been ensured by Bulgarian Development Bank and European Investment Bank and are part of the Investment Plan for Europe – one of the priority projects of the President of the European Commission *Jean-Claude Juncker*. The focus of the Plan is to promote investments in order to create jobs and achieve growth through a smarter use of new and existing financial resources, by removing barriers to investment and providing visibility and technical assistance to projects.

At the end of 2018, BDB concluded agreements with two commercial banks under the COSME+ Programme in support of small and medium-sized businesses, and launched lending for SMEs under preferential terms and conditions. The COSME+ Programme is implemented with support from the *European Fund for Strategic Investments for indirect financing of small and medium-sized enterprises with guarantee facility* and counter-guarantee. The COSME Programme builds upon the Entrepreneurship and Innovation Programme (EIP) launched in the period 2007-2013. The Programme's total budget amounts to EUR 2,300,000 thousand and covers the period 2014-2020. Four areas of support are included in its scope – improving access to finance for SMEs in the form of equity and debt instruments; improving access to SME markets worldwide; improving framework conditions for business competitiveness, and promoting entrepreneurship.

The implementation of the Leasing Line Programme directed towards partners – non-banking financial institutions – lessors registered with BNB and carrying out finance lease activities continued in 2018 as well.

At the end of 2018, BDB launched a new programme for indirect support for SMEs through commercial banks and non-banking financial institutions. The programme is for indirect financing of farmers who are members of mutual credit cooperatives of private farmers. Its budget amounts to BGN 15 million. The loans are limited up to BGN 1,500 thousand and are extended for periods of up to 5 years.

In 2018, an application was drawn up for MFI JOBS to the EIF Programme – EaSi for the provision of micro-financing and financing to social companies, under which MFI will use guarantees up to 80% (with limit of payments) to extend loans up to EUR 25,000 and to finance social enterprises falling within the definition of the European Commission. The financing instrument is a continuation of the Progress Microfinance Facility launched in 2010 under which 50 000 micro-clients of JOBS were financed for the total amount of EUR 440,000 thousand. MFI has applied to EaSi Programme for guarantees in support of micro-financing and social entrepreneurship with a total portfolio amount of up to EUR 9,000 thousand (EUR 5,000 thousand for micro-financing and EUR 4,000 thousand for social entrepreneurship).

The Chairman of the Board of Directors and Chief Executive Director of the Bulgarian Development Bank, Stoyan Mavrodiev is the winner in the category “Finance and Insurance” at the Mr. and Mrs. Economics 2018 competition. This is the second award for Stoyan Mavrodiev from the prestigious contest, which is organized by the Confederation of Employers and Industrialists in Bulgaria (KRIB) and “Economics” magazine.

In 2018, the process of rebranding the Financial BDB Group began – election of new logo for the bank and its subsidiaries, including elaboration of a brand book. The upgrading of the corporate vision coincided with the 20th anniversary of the Bank. The creation of a new, unified vision of the Bulgarian Development Bank Group corresponds with the pace of development of the financial institution in fulfilment of its mission to be a partner of business in its growth, to contribute to its competitiveness in the future, and to facilitate the building of an ecosystem, which favours entrepreneurship.

EXAMPLES OF SUCCESSFULLY IMPLEMENTED PROGRAMS AND PROJECTS

Bulgarian Development Bank AD

In 2018 as well, the implementation of the **Energy Efficiency of Multi-Family Buildings National Programme** continued – Bulgarian Development Bank AD provides financing under the Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP) approved by Decree No 18 of 2 February 2015 of the Council of Ministers of the Republic of Bulgaria (the Program). The Programme has been oriented to the renovation of multi-family residential buildings with a main objective to secure better living conditions for the residents in the multi-family residential buildings, heat comfort and higher quality of living environment. The implementation of energy efficiency measures in multi-family residential buildings will contribute to higher level of the energy efficiency of multi-family residential buildings and energy costs decrease; improving the exploitation features for extending the life cycle of the buildings; and providing conditions of living environment in line with the sustainable development criteria.

The expected results and effects from the Programme are heat costs reduction for the households; improved residential infrastructure and change of the urban appearance; cleaner environment – reduction in greenhouse gas emissions (CO₂, etc.); extending the life of the building and increasing its value. The economic effect consists of giving more opportunities to business for Economic activity – designers, construction industry, companies for technical audits, companies for energy efficiency audits, materials. producers, etc., as also participation in the implementation of the Programme of small and medium-sized companies from all over the country. The Programme achieves also social effects by providing additional employment, establishing traditions in the management of multi-family residential buildings and increasing public awareness of the ways for energy efficiency enhancement. The program activities cover the entire territory of Republic of Bulgaria, within 265 municipalities. The financial resources set aside by the State budget for the Programme amount to BGN 2 billion.

Examples of projects financed by the bank:

- **Construction Company** with main scope of activity the development, construction and reconstruction of industrial and commercial buildings, production halls, factories, auto-repair shops, corporate buildings, store of large commercial chains, etc. The company has manufacturing facilities, specialist equipment and technical staff. It offers, together with other Group companies, “complete engineering” and „design and construction in one“. The completed projects are characterised by different design and operation conditions, high construction quality and are widely distributed and recognisable around the country – hypermarkets Billa, Metro, Hit, Praktiker, sports halls, Sofia Airport, etc. The company participates in joint projects with foreign investors – the German manufacturer Leoni, the Japanese corporation Yazaki.
- Licensed **air carrier** with basic products and services in the field of transport and charter services, “wet” lease (ACMI), “dry” lease, etc. The Borrower plans to expand business by purchasing aircrafts instead of leasing such.
- **A company operating the biggest mussels farm in Bulgaria.** The company is specialized in cultivation and production of environmentally clean Black Sea mussels, which it cultivates in its own plantation, which is the largest mussels plantation in the Black Sea. Its construction has gone through three main stages financed under the SAPARD Programme, the Operational Programme Fisheries Sector Development (OPFSD) /2007-2013/ and Maritime and Fisheries Programme /2014-2020/. BDB has extended an investment loan to the company for the construction of the processing plant with technological equipment for processing, packaging, cooling and freezing of cultivated mussels.
- **A company registered as a farmer**, holding 300 decare of agricultural land in the areas of the Malko Gradiste village, with fully developed and operational pear garden on 170 decare with 19,809 pear trees,



equipped with an anti-hail system, a droplet irrigation system, bored well, and a water-main. The object of financing is the upcoming construction of warehouses for storage of plant production, agricultural equipment and machinery, office and household premises, which is the last stage of development of the whole farm. The project is supported by grants under Sub-measure 4.1 Investment in Agricultural Holdings by the Rural Development Programme (RDP) 2014-2020 on the basis of a contract signed with the State Fund Agriculture. The implementation of the project aims at reducing direct operating costs, achieving higher quantitative and qualitative production results, making better use of production factors, and in the end, achieving a cost-effective and competitive production of pears.

- **A company operating in the area of the Bulgarian printing industry**, which provides to its customers printing services of high quality, combining traditions and high quality. Investments in the company have been made also with the support of the European Regional Development Funds (the company implements two Phase projects under the under the pre-accession programmes – Leonardo da Vinci programme, the Innovation and Competitiveness Operational Programme). The overall objective of the projects implemented so far and the financial support rendered by the bank is to improve competitiveness and achieve sustainable growth by improving energy efficiency and expanding the production capacity of the company.
- **A factory for producing various types of paper, including tissue paper**, for industrial customers in Bulgaria and abroad. The company's corporate vision is to continuously invest in modernizing existing equipment and acquiring new production facilities. Over the last two years, the company has been implementing an investment program to reduce the specific consumption of resources per tonne of product manufactured, as well as acquiring various peripherals to existing machines, allowing automation and computer assurance of the production process and thus, increasing quality control.
- **A holding group of companies in the IT sector**. In recent years, the company has been gradually acquiring various companies, including such with over 17 years of experience and start-ups. In 2016, the holding established a subsidiary in Nish, Serbia. The holding has, through its network of companies, 8 offices situated in 7 cities – Plovdiv, Sofia, Veliko Tarnovo, Varna, Blagoevgrad, Svishtov, and Nish. The main groups of services are in the IT area: trade, consulting activity, software implementation and maintenance, advertising activities, business agency, patent acquisition, granting of licences, and others. A project of a group company for obtaining a grant under the Innovation and Competitiveness Operational Programme has been approved. BDB has extended a loan for working capital to finance marketing activities for restoring a client database. The expected effect is the continuing growth of new customers, adding to those already attracted in 2017 and the beginning of 2018 from Switzerland, USA, United Kingdom, and increasing the volumes being offered to traditional customers of the group companies. The group expects a serious increase in revenue from its internally-developed human resource management product over the period of the loan agreement.

Micro Financing Institution Jobs EAD

The subsidiary, MFI Jobs, completed a number of successful projects over the year:

- With the assistance of MFI Jobs, a client of the company launched **excursion tours** covering various archaeological sites and sightseeing on **certain routes in the Sofia city and subsequently, outside the capital city. The programs are innovative and implemented through** audio-guide devices rented out to tourists, who have the opportunity to follow the route independently and to listen to the information in their preferred language.



- MFI Jobs has financed a micro-enterprise operating in the **rent-a-car business** in the territory of Bulgaria. The financed project expanded the business by purchasing additional vehicles to enrich the car fleet and take on more orders.
- Another successful project of MFI Jobs is the financing of a laser engraving company to start its own **production of wooden boxes** in which mechanical barrel-organs are installed. The financing has made it possible for the company to eliminate its dependence on suppliers of such boxes, while shortening the time for delivery of the finished products to customers and accordingly, expanding the range offered.

National Guarantee Fund EAD

The past 2018 is a year during which NGF was able to consolidate the results achieved in 2017 – for the period, it generated new business in the amount of over BGN 220 million in the form of guarantees issued and guaranteed loans for more than BGN 520 million. 2017 was the year in which the NGF reported the largest volume of guarantees issued since its establishment (guarantees issued of BGN 223 million and guaranteed loans for more than BGN 500 million).

The volume of guarantees of BGN 200 million was achieved mainly through the NGF's own risk guarantee scheme: The 2017-2018 Guarantee Scheme (guarantees issued for BGN 200 million on loans amounting to BGN 481 million). Guarantees of BGN 14 million under loans amounting to BGN 29 million were issued under the Rural Development Program. The remaining credit guarantees have been issued under the new guarantee scheme of National Guarantee Fund EAD with a counter-guarantee under the COSME Programme of the EIF.

Overview of the economic environment and banking system in 2018

In 2018, the Bulgarian economy reported record low unemployment and a reduction in external debt. Bulgaria's GDP marks a peculiar record – the expectations are for BGN 108 billion, and for the first time in Bulgaria's new history, it exceeds BGN 100 billion. GDP growth during the year remains sustainable and outstripping that of the Euro area and the EU average values – at a level of over 3%. The main driver of GDP growth remains domestic consumption and the level and growth of average income is also high. If combined with the growth of energy prices on global markets and food prices during the first three quarters of the year, this justifies the inflation rate that is higher than that in the Euro area, the growth of which remains lower than the growth of average income.

By sectors, what mostly contributed for the growth of the Bulgarian economy during 2018 was the Real estate transactions sector – an increase by 9.3% compared to the end of 2017. The low interest rates on residential loans and the improving environment on the labour market are the instruments to the record-high growth in real estate transactions; however, the growth in construction has slowed down to 4.0% per year, indicating the cooling of the real estate market over the next few years. The services sector continues to report a serious growth, establishing itself as the most important sector of the economy for the country during the last years. The relative share of value added realised as a result of the activities in the services sector has grown to 73.5% vs. 70.7% in the same period of the previous year. The industry also registers growth both of the Gross Added Value (GAV) produced in the sector, and in sales, and is also one of the sectors, the main driver of the economic growth during the year. The agricultural sector is weaker 2018, after its record-high growth in 2017.

The maintenance of a relatively high economic growth for a second year in a row lead to further improvement of the situation on the labour market. According to data of NSI, during the fourth quarter of 2018 the level of unemployment dropped to 4.7%, i.e. it was by 1.0% lower as compared to the same quarter of 2017, and the employment ratio increased to 71.1% for population between 20 and 64 years of age or by 0.2 p.p. on an annual basis. The low increase in employment rate shows that the peak of economic activity of the population is very close to its maximum and the economy is beginning to suffer from a lack of staff. This poses challenges to competitiveness and requires measures to intensify growth. The average working salary for the country in December was BGN 1,205, or a nominal increase by 7.3%. The increase in the public sector is by 7.5% YoY, while in the private sector the growth is by 7.1%. The factors underlying the increase in salaries are the developing economy and intensive competition for experts on the labour market; these factors will continue to support a growth of salaries ahead of the inflation, and especially, the compensation for qualified experts. With respect to the above, the Government undertook measures in order to regulate state administration, as well as by making a proposal to the employers to make specific offers of employment to Bulgarians who are currently working abroad, but occupying positions that need lower than their own qualification.

In 2018, the trade deficit increased to BGN 6.7 billion, net exports by about 0.7%, including the export to EU member states by 10.1%. The reason for the export stagnation was the decrease of export volumes to third countries by 12.3%. The main reasons for the significant reduction in exports to third countries were the economic situation in Turkey, the reduction in exports to Russia by more than 50%, low sales volumes of fuel and a variety of finished products. Together with the increase in consumption, imports increased by 7.4%. The trade balance deficit has a negative contribution to the growth of the economy. The trend of increase in imports over the export of goods is likely to continue until the end of the projection horizon, which will lead to a smooth increase in the trade deficit until 2020.

In 2017, the process of reduction of the external debt of the country continues. As compared to 2017, the total gross external debt of the private sector had decreased by 0.8% to 52.8% of GDP, while the external debt of the public sector decreased by 1.0% to 11,6% of GDP. The amount of direct foreign investments in Bulgaria reached EUR 1.744 billion in 2018, being the highest level for the last four years.

The average annual inflation for the period January-December 2018 as compared to the period January – December 2017 was 2.8%. The main groups of goods, which contributed the most for increasing the overall price index during the period were fuels and foods. The biggest increase in prices was reported by the transport sector – about a 4.7% annual increase. It is expected that the inflation rate for 2019 will be about 3.0%.

Banking sector

The past 2018 was a success for the banking sector in Bulgaria, marked with record-high profits, growth and improvement of the quality of bank portfolios, as well as continuing consolidation in the sector.

DSK Bank EAD began a process of acquisition of 99.74% shareholding in Societe Generale Expressbank AD (SGEB), which was finalised in January 2019. The new bank will be a leader in terms of assets and deposits together with UniCredit. The full integration of both institutions is expected to end in 2020.

Eurobank Ergasias S.A. (“Eurobank”) announces the completion of the transaction in which its subsidiary bank Eurobank Bulgaria (Post Bank) acquired Piraeus Bank, a subsidiary of Piraeus Bank S.A. (“Piraeus Bank”). Thus, the estimated market share of Post Bank will reach more than 10% and therefore, the bank will rank the third in terms of credit portfolio. It is expected that the transaction will be finalised in 2019.

At the end of December 2018, the assets of the banking system amounted to BGN 105.56 billion, which represented a year-to-year increase of BGN 7.75 billion. Increases were observed in all groups of assets, except for financial assets, where there was a decrease by BGN 189 million. The greatest dynamics belonged to the loans and receivables – a growth by BGN 7.11 billion, and cash by BGN 826 million. The banking system's profit after taxes was record-high at the year-end, reaching BGN 1,68 billion. The high profit was due to growth in fees and commissions (increase by BGN 70 million compared to 2017), interest income (increase by BGN 66 million), and of the decrease in impairment expenses by BGN 266 million compared to 2017. The decrease in loans past due reduced the impairment expenses and contributed to the stability of the financial system.

Despite record-low interest rates on deposits, the level of attracted funds increased by BGN 6.0 billion in 2018, reaching BGN 89.7 billion. Deposit dynamics was mainly due to growth in household deposits by BGN 3.9 billion, as also in those from non-financial entities by BGN 1.1 billion. There was also an increase in deposits from other financial entities and general government. The reduction in unemployment rates and salary increases result in a growth in deposits, real estate transactions and domestic consumption.

In 2018, interest rates on deposits dropped reaching 0.13% for BGN deposits and 0.14% for EUR deposits. It was noted that banks did not demonstrate appetite for more deposit funds than existing customers and offered better conditions for new customers with short-term deposits. The reason for that situation is that the fee income is significant, which motivates the banks to attract new customers as a matter of priority. At the end of December, the deposit interest rates of the banking system for new businesses are lower for deposits with a term of over 1 year than for fixed-term deposits maturing from 3 to 6 months and from 6 months to 1 year.

In 2018, total loans and advances grew by BGN 7.5 billion, with increases being observed in all types of loans. The highest growth was reported by real estate loans – by 15.28% YoY. BNB warned of the risk of cyclical risks in case of future increases in interest rates or a weakening of economic activity. It is expected that increases in interest rates on loans will increase the costs of servicing these loans, which could potentially result in an increase in loans past due for over 90 days.

Interest rates on loans for new businesses, original maturity for non-financial entities, dropped by 0,22 p.p. to 3.48% for BGN loans and by 0.47 p.p. to 2.91% for EUR loans. There is a tendency that interest rates on BGN loans exceed those charged on EUR loans.

BDB compared with the banks operating in the country

As a result of the growth and the merger of UBB and CIBank in 2018, BDB climbed from 12 to 9 position in the Bulgarian banking system in terms of assets. The Bank marked a significant growth in 2018, while maintaining its stable capitalisation and key ratios.

Management of BDB expects that the key ratios of liquidity and capital adequacy will continue to exceed considerably the average ratios reported by the Bulgarian banking system, and the yield to remain around its current levels over 2019.

Overview of the activity and selected financial information

Operating results of the BDB Group

The Group of Bulgarian Development Bank AD continues to work actively towards the objectives set, while maintaining high levels of liquidity and capitalization. The process of modernisation and updating the BDB's operations continued throughout 2018 as well, while the Bank continued to increase the volume of its activity.

Key financial ratios as of 31 December 2018 semicolon:

Comprehensive income	2018	2017	Change YoY
Net interest income	57,166	57,666	(-1%)
Net fee and commission income	5,610	4,842	16%
Net gain on foreign currency transactions	379	409	(-7%)
Net income from financial assets measured at fair value through other comprehensive income	738	188	293%
General and administrative expenses	(25,618)	(18,399)	39%
Other operating income / (expenses)	669	391	71%
Income before impairment	38,944	45,097	(-14%)
Income from reversed / (expenses on) impairment and provisions	(10,046)	(22,095)	(-55%)
Profit before taxes	28,898	23,002	26%
Income tax expense	(1,811)	(2,322)	(-22%)
Net profit for the period	27,087	20,680	31%
Actuarial gains / (losses) on defined benefit plans, net of taxes	33	(63)	(-152%)
Net change in the fair value of financial assets measured at fair value	(343)	4,469	(-108%)
Total comprehensive income	26,777	25,086	7%

The 2018 net interest income marked a minimal drop by 1% less versus 2017 amounting to BGN 57,166 thousand (as of 31 December 2017: BGN 57,666 thousand) with the main reason underlying this result being the environment of lower interest rates on loans. Net fee and commission income increased by 16%, or by BGN 786 thousand in nominal terms.

General and administrative expenses (incl. depreciation/amortisation) grew from BGN 18,399 thousand to BGN 25,618 thousand, with the main reason being the increase of the contribution to the Fund for Orderly Bank Restructuring more than twice up to BGN 6,913 thousand (2017: BGN 3,180 thousand).

The financial result after taxes of Bulgarian Development Bank as of 31 December 2018 was a profit of BGN 27,087 thousand compared to BGN 20,680 thousand in the previous year, or a growth by 31% for 2018.

The effect of the initial adoption of IFRS 9 amounts to (BGN 11,637 thousand) and was reported in *Reserves from subsequent valuation of financial assets measured through other comprehensive income* and *Other reserves* as at 01 January 2018.

Financial performance	As at 31 December 2018	As at 31 December 2017	Change YoY
Assets			
Cash in hand and balances in current account with the Central Bank	297,622	447,648	(-34%)
Receivables from banks	430,003	198,910	116%
Financial assets at amortised cost	1,530,249	1,446,627	6%
Financial assets at fair value through other comprehensive income	653,657	291,867	124%
Fixed assets	37,597	32,999	14%
Other assets	44,365	40,550	9%
Total assets	2,993,493	2,458,601	22%
Liabilities			
Deposits from credit institutions	5,759	33,909	(-83%)
Borrowings from international institutions	904,782	869,822	4%
Deposits from customers other than credit institutions	1,171,825	659,847	78%
Other borrowings	110,331	111,406	(-1%)
Other liabilities	10,630	8,793	21%
Total liabilities	2,203,327	1,683,777	31%
Equity			
Issued capital	601,774	601,774	0%
Retained earnings	27,087	21,995	23%
Reserves from subsequent valuation of financial assets measured through other comprehensive income	10,909	11,003	(-1%)
Other reserves	150,396	140,052	7%
Total equity	790,166	774,824	2%
Total liabilities and equity	2,993,493	2,458,601	22%

As at 31 December 2018, the Group's assets amounted to BGN 2,993,493 thousand, growing by 22% y-o-y (2017: BGN 2,458,601 thousand).

Banking Activity of the Group – Bulgarian Development Bank

- The financial result after taxes of Bulgarian Development Bank as of 31 December 2018 was a profit of BGN 25,130 thousand compared to BGN 20,145 thousand in the previous year, or a growth by 25% for 2018. As of 31 December 2018, Bank's assets amounted to BGN 3,012,761 thousand, a 22% growth compared to the previous year. The main driver of the asset growth was;
- The increased direct lending, which reached BGN 1,039,080 thousand as of 31 December 2018 (compared to BGN 699,680 thousand as of 31 December 2017), or a growth of 49%;
- The investments in securities that have grown to BGN 594 249 thousand as of 31 December 2018, or a growth of 157%;
- The growth in loans to other banks.

These movements were partially offset by the drop in assets under the Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP) (a balance of BGN 471,999 thousand at the end of 2018 vs. BGN 728,010 thousand at the end of 2017) and the reduction in over-reserves deposited with BNB; the remaining part of this growth is financed by the higher amount of deposits from other customers and international institutions.

The credit activity of BDB consists of both direct lending and indirect financing through programs for funding commercial banks, which use the received funds to provide loans to SMEs and agricultural producers, i.e. the so called on-lending.

In 2018, the Bank continued to actively develop its business, supporting Bulgarian businesses, continuing to maintain a diversification of the industry structure of its loan portfolio. Greater dynamics are observed in the relative shares in the credit portfolio of the following sectors: Industry (increase by 45%), Tourist services (growth of 564%), Financial services, and General government enterprises. (Note 18B to the annual financial statements).

The Group's activity related to micro-lending through MFI Jobs

In 2018, financing of BGN 3,094 thousand was extended to end customers under 36 loan and lease agreements.

The company's active loan and lease portfolio amounted to BGN 15 530 thousand (at amortised cost before impairment) and comprised 349 loan and lease transactions as at 31 December 2018. The company also has receivables from 12 non-profit partnerships amounting to BGN 466 thousand before impairment.

The 2018 financial result is a pre-tax profit of BGN 124 thousand.

The 2018 total revenue of the company amounts to BGN 1,484 thousand, including interest income of BGN 1,412 thousand or 95% of total income.

The Group's activity related to guarantee schemes through NGF

The primary goal of the National Guarantee Fund is to ensure guarantees in favour of SMEs and thus, to facilitate their access to financing.

The guarantee issued by the Fund at its own risk may cover up to 50 percent of the liability. Following an amendment to the Bulgarian Development Bank Act, promulgated in State Gazette, issue 102 of 21 December 2012, the guarantees issued by NGF EAD in relation to the guarantee schemes under both, the Rural Development Program 2007 – 2013 and the Operational Program Fisheries Sector Development 2007 – 2013, the guarantees may cover up to 80 percent of the liability.

From the start of its operations in 2008 to the end of 2018, NGF EAD has implemented 9 guarantee programs and issued guarantees in the amount of BGN 1,122 million. The funding used by SMEs with the support of NGF includes guaranteed loans totalling BGN 2,365 million. The SMEs receiving support are over 9,100.

The first guarantee scheme of NGF – **Guarantee Scheme 2009-2013** began in 2009 and loans were concluded until February 2013. Agreements with 11 commercial banks were signed under the first guarantee scheme. According to the scheme, NGF issues guarantees under loans to SMEs amounting to BGN 500 thousand on investment and working capital loans, as well as bank guarantees. The maximum amount of the guarantees is up to 10 years. NGF approves the inclusion of loans to the guaranteed portfolio on an individual basis. Guarantees of BGN 168,000 thousand on loans amounting to BGN 391 thousand were approved by NGF within the time limit for inclusion of loans to the guaranteed portfolio. The total number of the enterprises supported under the scheme reached 2,325. The book value of the Fund as at 31 December 2018 was BGN 2,661 thousand.

Only new loans to small- and medium-sized enterprises are included in the guaranteed portfolio under **Guarantee Scheme 2014-2015** with a maximum amount of the guarantee provided by NGF EAD covering up to 50% of the loan amount, but not more than BGN 500 thousand. The guarantees issued over the period of inclusion of loans to the program from March 2014 to September 2015 amounted to BGN 87,000 thousand under loans amounting to BGN 200,000 thousand. The SMEs supported were 770, of which half were micro-enterprises, 40% were small-sized enterprises and 10% were medium-sized enterprises. The guarantee matured in September 2018 and at the reporting period-end, there were no portfolio under this scheme. As a matter of comparison, the guarantees approved as at 31 December 2017, which were included in the portfolios of the partner banks, amounted to BGN 49,047 thousand and the guaranteed debt amounted to BGN 39,009 thousand, respectively.

From the beginning of October 2015 to the beginning of January 2016, guarantee agreements totalling to BGN 326,000 thousand were signed between NGF EAD and 10 commercial banks under the **Guarantee Scheme 2015-2017**. According to the scheme, NGF guarantees up to 50% of the loan amount, but not more than BGN 1 million. The time limit for inclusion of loans in the guaranteed portfolio ended on 31 March 2017. Until the expiry of the time limit for inclusion of loans in the guaranteed portfolio, 31 March 2017, NGF EAD provided to 2,024 SMEs guarantees of BGN 258,080 thousand on loans amounting to BGN 581,500 thousand. The amount of the guarantees approved, which were included in the portfolios of partner banks as at 31 December 2018, was BGN 169,775 thousand and the amount of the guaranteed debt was BGN 125,705 thousand.

In March and April 2017, guarantee agreements totalling to BGN 328,000 thousand were signed between NGF EAD and 10 commercial banks. **The Guarantee Scheme 2017-2018** is a continuation of NGF 2015. According to the scheme, up to 50% of the loan amount is guaranteed, but not more than BGN 1 million. The time limit for inclusion of loans in the guaranteed portfolio ended on 30 September 2018. Since the start of the Guarantee Scheme until 31 December 2018, 3,000 SMEs have been supported and guarantees of BGN 323,583 thousand have been issued. The amount of the guarantees approved, which were included in the portfolios of partner banks as at 31 December 2018, was BGN 323 528 thousand and the amount of the guaranteed debt was BGN 292 993 thousand.

The guarantee program in support of beneficiaries under **Operational Programme Fisheries Sector Development 2007-2013 (DFSOP)** is a financial engineering instrument and a process for the issuance of guarantees to supplement the collateral on loans extended by banks to borrowers for the purpose of implementing projects approved under the following DFSOP measures:

Measure 1.3: Investments on board fishing vessels and selectivity

Measure 2.1: Productive investments in aquaculture

Measure 2.5: Inland Fishing

Measure 2.6: Investments in the processing and marketing of fishery products and agriculture

Measure 3.3: Investments in reconstruction and modernisation of fishing ports, landing sites and shelters

And also under Priority axis 4: Sustainable development of fisheries areas of projects of some of the beneficiaries under the Priority axes One, Two and Three and all beneficiaries under the Priority axis Four of DFSOP.

With the support of the scheme, projects valued at BGN 46,000 thousand were implemented, of which projects worth BGN 33,000 thousand were under measure 2.1 (79% of the measure's budget); under measure 2.6, projects worth BGN 12,000 thousand (77% of the measure's budget) were supported. Projects for BGN 500 thousand were supported under Measure 4.1. 25 SMEs were supported. The book value of the guaranteed debt as at 31 December 2018 was BGN 3,848 thousand.

The guarantee program in support of beneficiaries under **Rural Development Programme 2007-2013 (RDP)** is a financial engineering instrument approved by the Eight Amendment to the RDP and a process for the issuance of guarantees to supplement the collateral on loans extended by banks to borrowers for the purpose of implementing projects approved under Measure 121 Modernisation of agricultural holdings, Measure 122 Improvement of the economic value of forests, and Measure 123 Adding value to agricultural and forestry products of RDP of the Republic of Bulgaria (2007-2013).

Guarantees of BGN 185,606 thousand on loans amounting to BGN 238,111 thousand were approved by NGF within the time limit for inclusion of loans to the guaranteed portfolio. Under the scheme, 554 beneficiaries were supported under the program for the implementation of projects amounting to BGN 375,000 thousand. The book value of the guaranteed debt as at 31 December 2018 was BGN 14,692 thousand.

The guarantee program in support of beneficiaries under **Rural Development Programmes 2007-2013, 2014-2020, and enterprises operating in the sectors of Crop and Animal production – Guarantee scheme – MAF 2016-2018**, is a joint initiative with the MAF, which is implemented using funds released from the Guarantee Scheme under RDP 2007-2013 amounting to BGN 50 million. During the second quarter, NGF and MAF agreed upon the parameters of the new guarantee scheme and invitations were sent to the commercial banks to take part in the scheme. Agreements with 17 commercial banks and MFI Jobs were signed under the guarantee scheme, whereas part of the BDB Group provides financing up to BGN 300 thousand. Since the start of the scheme until 31 December 2018, NGF issued guarantees of BGN 61,540 thousand under loans amounting to BGN 123 755 thousand. The book value of the guaranteed debt as at 31 December 2018 was BGN 38,533 thousand. SMEs supported were 96.

Guarantee scheme under the COSME Programme of the European Commission – in December 2016, an agreement was signed between the European Investment Fund (EIF) and National Guarantee Fund EAD (NGF EAD), by virtue of which another EUR 40 million was ensured for financing Bulgarian small- and medium-sized enterprises under the COSME Programme of the European Commission. The funds have been provided with the support of the European Fund for Strategic Investment (EFSI), on which the Investment Plan for Europe (the “Juncker Plan”) is based. EIF ensures a guarantee line of EUR 20 million, by which NGF will support an EUR 40 million financing to SMEs in Bulgaria that experience difficulties in ensuring collateral required. At 31 December 2018, NGF EAD has signed agreements with Bulgarian-American Credit Bank AD, TBI Bank EAD, MFI Jobs EAD, First Investment Bank AD, and Eurobank Bulgaria AD. 118 SMEs were supported.

At 31 December 2018 there were 76 loans guaranteed for the total amount of BGN 17,701 thousand. The book value of the guaranteed debt at 31 December 2018 was BGN 8 636 thousand.

Guarantees under micro-credits issued by Bulgarian Development Bank and administered by NGF EAD – The transfer of the Micro-credit Guarantee Fund Project from the Ministry of Labour and Social Policy to Bulgarian Development Bank AD was carried out on the grounds of §2 of the Transitional and Final Provisions of the Bulgarian Development Bank and Decision 309 of 3 May 2007 of the Council of Ministers of the Republic of Bulgaria. After the approval of the project by the Group of BDB AD, NGF was assigned with the task to administer the guaranteed loans. The loans extended under the Micro-credit Guarantee Fund Project at 31 December 2018 are administered by BDB AD.

The 2018 financial result after taxes from the activity of National Guarantee Fund EAD amounted to BGN 2,512 thousand.

Considering the results from the risk assessment testing of the guaranteed portfolio at the end of 2018, the NGF's management decided to reduce the portfolio's coverage for expected credit losses from 1.46 % in 2017

to 1.09 % in 2018 in accordance with the commitment taken by NGF EAD. In view of the guaranteed portfolio risk assessment, the provisions set aside ensure an adequate coverage for expected credit losses.

- The 2018 Fund's revenue amounts to BGN 5,108 thousand (an increase by 2.9% compared to 2017) and originates from two main sources income of BGN 1,474 thousand on the Fund's capital invested in deposits and government securities;
- Fee and commission income of BGN 3,625 thousand on guarantees issued;

The main expenses incurred by the Fund in 2018 are administrative expenses amounting to BGN 1,474 thousand.

An impairment of BGN 1,658 thousand accrued on guarantees paid and a reversal of expected credit losses on guaranteed portfolios of BGN 709 thousand were reported over the period.

Development strategy

BDB – together with the Group companies – is a key instrument and channel for conducting government economic policies, including in specific areas, regions, industries and social groups. The Bank and the Group companies actively collaborate with all government state structures in order to ensure maximum impact of the public funds targeted on support of the economic development. The focus of the activity is pre-export, export and bridge financing.

BDB and its subsidiaries operate in full transparency and apply the best banking and management practices. A core objective of the Bank is to reach the sectors of the economy and borrowers experiencing difficulties in accessing and obtaining financing, by providing financial solutions and products to overcome market imperfections.

In pursuing its mission, BDB – jointly with Group companies – supports government efforts for acceleration of economic growth in the country by means of providing expertise and performing activities in all area of economic policies, facilitating the absorption of the EU structural funds, enhancing the export potential of the country, financing public and public-private project or partnerships of strategic national or regional importance, incl. infrastructural projects, etc.

The main principle underlying the BDB Group's activity is not to allow distortion of competition and crowding out of the traditional commercial banks from the market. By compensating any existing market failures in financing certain segments and clients, BDB and its subsidiaries contribute to adjusting their risk profile and further facilitates the increase of bank mediation and growth in credit volumes in the economy.

The strategic goals of the BDB Group are:

- To facilitate the economic growth by supporting regions and sectors of the economy with established market shortage and potential for growth;
- To stimulate the economic activity of the investors for the modernization of the material and technological basis and for boosting the competitiveness of the economy;
- To facilitate the economic growth of the regions through financing, including syndicated, of sizable, strategic and infrastructural, by their nature, projects and investments;
- To support the development of competitive production initiatives and sectors of the economy of proven export potential;
- To facilitate, jointly with the other institutions in the country, the access to financing of innovative and newly established companies (start-ups);
- To facilitate and support the direction of capital flows to the Bulgarian economy.

In planning and carrying out its operational objectives, the BDB Group will maintain the two approaches to support SMEs in the country – through direct lending and through indirect programmes through commercial banks. BDB follows the principles of prudent risk assessment and adequate management of these risks.

With regard to direct lending, the Bank will further develop focused product lines related to SME support. To fulfil the objectives, priorities will be pre-export, export and bridge financing. Traditionally, BDB will continue to provide financing for small and medium-sized businesses with a longer loan period and relieved legal requirements for loan collateral.

The Bank Group considers that, in a context of high liquidity in the banking sector, the absorbing of part of the risk, namely additional risk that discourages commercial banks from financing, would be a key factor in the success of indirect programmes.

The Bank, together with the Group entities, will collaborate with the management bodies of the operational programs in Bulgaria, by identifying existing financial gaps of specific measures and will propose solutions to resolve them, including specific forms of financing. Further consultations will be carried out in order for BDB to become an integrated part of the overall model of managing public resources for the support of the real economy. The Bank considers its participation as an essential step in the improvement of the effectiveness of measures in support of the Bulgarian economy.

The BDB Group will continue to support initiatives of the Bulgarian state in support of the economic and social development of the country. In 2019, BDB will continue in implementing the Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP).

In 2018 and early 2019, BDB incorporated new subsidiaries with objects of activity: equity investments in shares of other companies, leasing and factoring. The aim is to expand the financial services and solutions offered, and to meet the demand for these products on the main market segments.

Development of Bulgarian Development Bank AD in 2019

Key strategic goals and policies of the Bank within the 2019-2020 horizon will be as follows:

- Continued growth of financing to support the development of the national economy and the realization of the Government's economic priorities;
- Realization of a sustainable process in the creation and development of targeted product lines under the two main approaches for SME financing;
- Conservative assessment of risks and maintenance of high level of coverage of problem loans by provisions.

The Bank intends to significantly diversify its funding sources. Bond instruments are to be used in the formation of liability where balancing, in terms of the international and the domestic market, will be made currently and depending on the specific market conditions.

BDB intends to apply for the role of a direct guarantee implementing partner of the Invest EU Program, a program that is to be a major channel for business support in the next EU programming period.

Development of National Guarantee Fund EAD in 2019

The main goals set by the Fund for 2019 are:

- Effective implementation of guarantee programs to support enterprises in the Agriculture, Forestry and Fisheries sector through guarantee schemes under the Rural Development Program 2007-2013, 2014 – 2020, and for enterprises in the Crop and Animal Production sectors.

- Continue active work on implementation in the practice of the guarantee programs in support of micro-, small- and medium-sized enterprises in the Republic of Bulgaria;
- Organisational and technical development of the NGF's structure in the context of new engagements;
- Optimisation and improvement of the procedures employed by the Fund.

In order to fulfil its goals and tasks, NGF EAD will work closely with partner banks on guarantee agreements, and with national and European authorities and institutions directly involved in the implementation of the financial engineering schemes; moreover, the Fund will make efforts to attract new partners and will seek the cooperation of small- and medium-sized business associations at national and regional level.

Development of Micro Financing Institution Jobs EAD in 2019

Management of **Micro Financing Institution Jobs EAD** is committed to achieving future sustainable development of the company's activity and growth of its assets.

Internal control

The internal control processes within the Bank and Group companies include the following components:

- (a) Control environment – a description of the control environment can be found in items Risk Management, Control Environment, and in the Corporate Governance Statement, Control Environment section of this Report.
- (b) Risk assessment process – a description of the control assessment of the risks may be found in Corporate Governance Statement, Risk Management and Control Environment section;
- (c) Information system, information system, including the related business processes relevant to the financial reporting, and communication – description of the information system of the Bank may be found in the Risk Management sections of this report;
- (d) Control activities – a description of the control activities may be found in the Risk Management section, part of Corporate Governance Statement, Structures for Risk Management and Committees to the MB sections;
- (e) Ongoing monitoring of controls – a description of the ongoing monitoring and control may be found in Corporate Governance Statement, Structure for Risk Management and Committees to the MB sections.

Risk management

In managing its risk, the BDB Group applies policies and procedures based on best practices and appropriate to the nature and complexity of its activity. In the course of the ordinary activity, the companies from the Group are exposed to various financial risks, the occurrence of which may lead to losses and to deterioration of the financial stability of the institution. These risks are identified in order to be managed and to avoid any unjustified concentration of a particular risk. The risk management process is important for profitability and for its existence. The most significant risks, to which the BDB Group is exposed, are following credit, market and operational risks.

Credit risk

The credit risk is the key risk to which the BDB Group is exposed, and therefore, its management is a key priority of the activity. The credit risk management takes place in compliance with the BDB Act, and the effective statutory laws and regulations of the Republic of Bulgaria, regulating the credit activity, the established international norms and best banking practices. The BDB Group applies internal rating for the evaluation and management of the credit risk (incl. from counterparties) under the exposures. Bodies for monitoring, control and assessment of the quality of the credit portfolio have been created and are functioning at the Group. Procedures and mechanisms have been introduced for ongoing monitoring, recording and management of the credit portfolio, requiring periodic, and if necessary, extraordinary reports on the financial and legal status of each borrower and the physical bodies in debt. When new circumstances are established, which may lead to a change to the risk profile of the borrowers, including to increasing the risk of non-collectability of the credit exposure, adequate measures, which are in line with the risk parameters of the debtor, are undertaken. When managing the credit risk, the BDB Group follows a system of internal bank limits by economic sectors on a consolidated basis, by

instruments, as well as other credit limitations and thresholds for concentration, and the results from the monitoring of their compliance are reported to the competent bodies. The system of limits is reviewed and updated periodically.

Market risk

In managing the currency risk, the BDB Group follows the principle of maintaining minimum open FX positions through the observing of established limits. The positions in various currencies, as well as the general FX position are monitored on a daily basis. The FX positions are not formed for speculative purposes, but are the consequence of the currency transactions, occurring in the course of the ordinary bank activity. These FX transactions relate to the current needs of financing the position. In managing its assets and liabilities, due to the specifics of its financing, the Group seeks to maintain these assets and liabilities in EUR or BGN. The open FX position takes into account the terms and possibilities for netting the EUR and BGN positions in accordance with the applicable regulatory framework.

Regular reports, distributed periodically according to their sensitivity to changes in the interest rates, are prepared on the financial assets and liabilities in order to manage the interest risk. A system of limits was introduced in connection with the fluctuations in the interest curve, while stress scenarios are applied to the discrepancies by periods, thus estimating the potential risk for the interest revenues and the capital of the BDB Group.

The assumption of risks when transacting on the money and capital markets is managed by a system of limits reflecting the risk profile of the investments. These limits are determined according to parameters of the portfolio, like counterparty, financial instrument, maturity, etc. The system of limits is periodically reviewed, while the compliance with the limits is subject to daily monitoring. The securities portfolio, created by the BDB Group in order to invest the available funds, is characterized by a relatively low interest rate risk and comprises relatively liquid government securities and securities issued by reliable institutions, i.e. low price risk. Due to the absence of a trade portfolio pursuant to the statutory regulations, the Group does not allocate capital for market risk.

The liquidity of the BDB Group is managed by strictly monitoring the ratios, indicating the liquidity position by periods. The liquidity risk is measured by applying additional scenarios for the cash flows from operations. In addition, the liquid buffers are measured and monitored, as well as the additional sources of financing upon market and idiosyncratic shocks. The observing of the limits for liquidity ratios is monitored and reported regularly before the relevant competent bodies.

Operational risk

The operational risk is managed by strictly monitoring and registering all operational events occurring in the activity of the various units as a result of the processes within the BDB Group. Operational events, which are more frequent, and the ones having great potential or real impact on the financial result, are subject to strict investigation and monitoring. They serve as the basis for the analysis of the operational risk in various scenarios, including operational risk stress tests. The operational risk is measurable and controllable, while a registry of the operational events is maintained and used as basis for analysis and improvement of the bank's working processes and for minimizing the conditions, which could potentially lead to operational events and loss for the Group. The necessary capital for operational risk is calculated by using the basis indicator approach pursuant to the applicable regulatory framework.

Recovery Plan (Directive 59/15.05.2014/EU)

BDB has developed a Recovery Plan of the BDB Group. Its latest update, approved by decision of the MB No. 67 of 26 October and decision of the SB No. 39 of 30 October 2018, was submitted to BNB within the required deadlines. The Plan complies with the requirements laid down in the Law on the Recovery and Resolution of Credit Institutions and Investment Firms Guidelines on recovery plan indicators, and Technical advice on critical functions and core business lines of the European Banking Authority.

The Recovery Plan addresses the systemically important/critical functions of the BDB Group and sets out the recovery indicators – a system of indicators that Bank observes with the aim of early identification of potential situations which could jeopardise the financial performance of the institution. The prerequisites for the implementation of the recovery measures set out in the Recovery Plan are described. Scenarios and recovery options are considered which, in the event of activation of the Recovery Plan, can be taken, as well as the internal communication and decision-making process. A communication action plan has been elaborated in case of activation of the Recovery Plan.

The recovery plan is updated once a year and proposed for validation by the MB and SB of BDB. Furthermore, the Recovery Plan is updated in the event of a material change in the legal or organisational structure, activity or financial position of the Bank, or in the financial system in Bulgaria, which may have a significant impact on its effectiveness.

Control environment

The BDB Group follows management philosophy and operating style, subject to the principles of conservatism when performing the strategic goals set forth by the BDB Act.

The Bank, together with the other Group entities, applies the model of the three lines of defence within the risk management:

The first line of defence is the management control that the leaders of the operational units are exercising. The operational management identifies, evaluates, controls and mitigates risks, ensuring that they operate in accordance with the objectives set out in advance.

The second line of defence is the risk management and compliance function carried out by the Risk Management, Compliance and the Classified Information Departments with regard to the prevention of money laundering and terrorist financing. In their activities, these departments are supported by Management, Analysis and Regulation and Legal Departments. The second line of defence is independent from the first one in terms of organisation, and carries out preventive and ongoing control.

The third line of defence is the internal audit function. Internal Audit of the Group Department carries out ex-post control and provides assurance to senior management with respect to the effectiveness of risk management, internal control and corporate governance, as well as the way in which the first and second lines achieve the risk management and control objectives. Internal Audit of the Group Department provides comprehensive assurance from the position of the highest level of independence in the organisation, through a direct subordination to the Supervisory Board (SB).

Management assigns powers and responsibilities for the operating activity in line with a detailed internal normative set of documents, which are in conformity with the current national and European legislations, where in order to guarantee the relationships in accountancy and reporting, and various specialized committees, by hierarchy of authorities, were formed to the MB and SB of BDB as stated in the Corporate Governance Statement, being part of the current financial statements.

The BDB Group has developed an internal set of documents, which includes policy and communications focused on ensuring that all employees understand the goals of the Group, knows how individual actions are interconnected and contribute towards these goals, and who and how is reporting and what is their responsibility.

The BDB Group has implemented an information system, including business processes related to it, providing the necessary quality and control of the financial accountability and communication.

The Bank's audit committee monitors the financial reporting processes, the effectiveness of internal control systems and the effectiveness of risk management systems; moreover, it monitors the independent financial audit, conducts a review of the independence of the registered auditor, and makes recommendations for selecting a registered auditor.

Bank supervision authorities pursuant to the bulgarian legislation

In compliance with the requirements of the framework of the laws and by-laws, regulating the banking activity in the country, the BDB Group must follow limitations, related to certain ratios. As of 31 December 2018, the Group had observed all regulatory requirements of BNB and the Bulgarian legislation.

The capital adequacy ratio on a consolidated basis as of 31 December 2018 was 36.08% (31 December 2017: 49.63%). The coverage of assets with capital buffers exceeds by many times the statutory requirements. BDB continues to maintain a good liquidity level. The liquidity coverage ratio (according to the definition of Regulation 575 /2013/EU, LCR) of the Bank increased to 1,293% as of 31 December 2018 (compared to 291% at the end of 2017).

International cooperation

BDB and its Group subsidiaries continue to develop successful partnerships with leading European and international financial institutions, including through participating in specialized associations. This cooperation enables the Group to take advantage of the best banking practices, know-how, information on financial products, and also to participate in their development and imple

- BDB has direct access to up-to-date general and specific information about the latest changes in the legislative framework at European level and its implementation in the area of the development banks, and has the opportunity to participate in the process of negotiating these amendments. The membership in international specialized associations allows BDB to take part in seminars and meetings with the European Commission and its Directorates.
- Since 2005 BDB is an active member of the European Association of Public Banks (EAPB). The membership in EAPB contributes for the exchange of experience and best practices between BDB and the European public banks.
- Since 2007, BDB is a full member of the Network of European Financial Institutions (NEFI), including representatives from 19 institutions from various European countries. The mission of NEFI is to improve the exchange of information and ideas in order to facilitate SME's access to financing.
- In 2018, BDB continued its participation in the activity of the European Association of Long-term Investors (ELTI). BDB is a co-founder of this organization.
- In 2018, BDB was the first President by rotation and took the host's role at the First International Meeting of the China-CEEC Interbank Association of China and the Central and Eastern European countries. In

the framework of the meeting, at the beginning of July 2018, on a bilateral basis, BDB and the Chinese Development Bank (CDB) signed a financial cooperation agreement under the One Road, One Belt initiative. BDB is a co-founder of the China-CEEC Interbank Association of China and the Central and Eastern European countries.

- BDB is a shareholder of the European Investment Fund (EIF) and regularly participates in the discussions of the Group of Financial Institutions – shareholders, where the guidelines for development of the activities and policy of EIF are discussed. BDB regularly votes on various topics – the admission of new shareholders and other organizational matters.

Corporate governance of the BDB group

Bank Governance

There were no charges in the main BDB corporate governance principles in 2018.

Bulgarian Development Bank AD has a two-tier corporate governance structure, which consists of Supervisory Board (SB) and Management Board (MB).

Supervisory Board (SB) of BDB:

Luchozar Borisov – Chairman of the SB

Luchozar Borisov was born in 1978 in Samokov. He completed his Master studies in Macroeconomics and Accounting and Finance at the University of National and World Economy (UNWE). He has several specializations in Bulgaria and abroad, including in Entrepreneurship and Risk Capital in AUBG, Project Management in WIFI, Austria, Encouragement of Foreign Direct Investments in JICA, Japan, Stock-exchange and Banking in CITIBANK, etc. He has rich experience in corporative management. Mr. Borisov has been part of the management of both private and state-owned companies in the Industry, energy and financial sectors. Currently he is a Deputy Minister of Economy.

Mitko Simeonov – Deputy Chairman of the SB

Mitko Simeonov has a Master degree in Law from the New Bulgarian University and a Master degree in International Economic Relations from the University of National and World Economy. He also holds a postgraduate degree in financial management from the University of National and World Economy. He was Deputy Executive and Executive Director of the Agency for Privatization and Post-Privatization Control.

Velina Burska – Member of the SB

Velina Burska has a Master Degree in Economics and Organization of Internal Trade from the University of National and World Economy. From 2002 to 2017 she was the director of the Post-Privatization Control Directorate at the Agency for Privatization and Post-Privatization Control.

Management Board of BDB:

Stoyan Mavrodiev – Chairman of the Management Board and Chief Executive Director

Stoyan Mavrodiev holds a Master degree in Law from Sofia University “St. Kliment Ohridski” and a Master degree in Finance from the University of National and World Economy. He attended a series of courses at the International Tax Academy in Amsterdam, and has also trained in the US Department of State’s International

Program of Leaders. His career started as a legal, tax and business consultant at PricewaterhouseCoopers. In the period 1996-2006, he worked as a financial and legal consultant in the United Consulting, which he also managed. From 2009 to 2010 he is Deputy Chairman of the Commission for Economic Policy, Energy and Tourism and member of the Budget and Finance Committee of the 41st National Assembly. For 6 years (2010-2016), he is Chairman of the Financial Supervision Commission (FSC), which oversees and regulates the financial system and the non-banking financial sector in Bulgaria. From 2010 to 2016 he is a member of the Advisory Financial Stability Board (FSF). In this period, it is also a member of a number of international organizations, including ESMA, EIOPA, ESRB, IOSCO, IAIS and IOPS.

Rumen Mitrov – Deputy Chairman of the Management Board and Executive Director

Rumen Mitrov holds a Master of Accounting and Control from the University of National and World Economy. His professional experience began in 1994 at NRA Sofia. In the period 2000-2003 he is the manager of the petroleum products import company “GMN GAZ”, and from 2003 to 2011 he is engaged in financial and tax consultancy as manager of the two accounting companies “Eurotim Bulgaria” and “RM Consult”. From 2011 to 2016, he was consecutively appointed Director of “Investment Activity Supervision”, “Regulatory Policy”, and “Coordination, Analysis and Policy of Supervisory and Supervision Activities” divisions in the Financial Supervision Commission (FSC).

Nikolay Dimitrov – Member of the Management Board and Executive Director

Nikolay Dimitrov holds a Ph.D. in Economics from the University of National and World Economy (UNWE) with specializations “International Economic Relations” and “Finance”. Between 2007 and 2015, he completed a number of additional courses and qualifications at the Judge Business School at Cambridge University (UK), the Investment Banking Institute (USA), among others. His banking career started at the end of 2003 and went through Raiffeisen Bank and United Bulgarian Bank. He joined the Bulgarian Development Bank in July 2011, in January 2012 become Head of the Investment Banking and Project Finance Department, and since April 2013 he is Head of the Corporate Banking Division. Alongside, he has been an associated professor at the Department of International Economic Relations at UNWE over the period 2010 – 2017.

Until 06 March 2018, Iliia Vasilev Kirchev was also a member of the Management Board of BDB.

Bulgarian Development Bank AD is represented by either two of the Chief Executive Director, Executive Directors and the Procurator, jointly.

Contracts signed with related parties involved in the management and participation of the Bank's MB and SB members in other companies

There are no contracts signed pursuant to Art. 240b of the Commercial Act between the members of the SB and MB or persons related to them, on one hand, and the Bank, on the other, which fall beyond the ordinary course of business or which deviate significantly from the market conditions.

In 2018, there were no concluded deals between BDB and its related parties, or offers for signing such deals, which fall outside the scope of the ordinary activity, or which significantly deviate from the market conditions, to which BDB or its subsidiary is a party.

There are no material contracts of the Bank, which lead to action, are amended, or terminated, due to change in the control of the Bank, when performing a compulsory public procurement procedure. As far as there is a legal restriction regarding the acceptable range of shareholders of BDB, pursuant to the BDBA, no such contracts are expected to be concluded.

The BDB Group does not have practice and has not concluded agreements between the companies and their Management bodies or employees for the payment of compensation upon resignation or dismissal without legal grounds thereof, or upon terminating the legal employment relationships by reasons related to tender offers.

A participation, pursuant to Art.247, Para.2, item 4 of the Commercial Act, of members of the SB and MB in commercial companies as general partners holding more than 25 per cent of the capital of another company, as well as their participation in the management of other business companies or cooperatives as procurators, managers or members of boards, is as follows (as of 31 December 2018):

- With respect to members of the SB of the Luchezar Dimitrov Borisov – Chairman of the SB – he participates in the management of Energy Efficiency and Renewable Sources Fund, UIC: 131330278, member of the MB of the company
- Mitko Emilov Simeonov – he has no participations in the capital and management of other companies
- Velina Ilieva Burska – she has no participations in the capital and management of other companies

With respect to members of the Management Board (MB) of the Bank:

Stoyan Todorov Mavrodiiev – Chief Executive Director, Chairman of the MB; he participates in the management of the following commercial companies:

- Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank, as Chairman of the Board of Directors and Executive Director;
- NATIONAL GUARANTEE FUND EAD, UIC: 200321435, a subsidiary of the Bank, as Chairman of the Board of Directors;
- REAL ESTATE VENTURES EOOD, UIC: 131160908, a sole equity owner.

Rumen Dimitrov Mitrov – Executive Director, Vice Chairman of the MB, he participates in the management of the following commercial companies:

- Micro Financing Institution Jobs EAD, UIC 201390740, a subsidiary of the Bank, as Vice Chairman of the Board of Directors;
- Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank, as Vice Chairman of the Board of Directors;

Nikolay Dimitrov Dimitrov – Executive Director, member of the MB; he participates in the management of the following commercial companies:

- Micro Financing Institution Jobs EAD, UIC 201390740, a subsidiary of the Bank, as a member of the Board of Directors;
- Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank, as a member of the Board of Directors;

Details about the full amount of the remuneration, rewards and/or benefits paid by the issuer and its subsidiaries to each one of the members of the management and control bodies for the reporting financial year are disclosed in Note 37 and Note 13A to the financial statements.

CORPORATE GOVERNANCE OF THE SUBSIDIARIES

BDB owned the following subsidiaries as at 31 December 2018:

- Sole owner of:
 - National Guarantee Fund EAD, UIC: 200321435;
 - Micro Financing Institution Jobs EAD, UIC: 201390740;
 - Maritsa Trade Center EOOD, UIC: 115619162

- Co-owner together with NGF of Capital Investments Fund AD, UIC: 205322014, with the distribution of the subscribed capital being as follows: (84.62% held by BDB and the remaining 15.38% held by NGF).

National Guarantee Fund

NGF EAD has a one-tier management system – Board of Directors, comprising three members. As of 31 December 2018, the composition of BD was as follows:

Board of Directors of the company:

Stoyan Mavrodiiev – Chairman of the Board of Directors

Angel Djalazov – Vice Chairman of the Board of Directors and Executive Director

Angel Djalazov has over 15 years of experience in international investment banking, asset management, capital markets, project finance, investment products, supervision and financial instruments management. He has occupied consequently the positions of an investment manager of TBD Fund, Director of Legal Department at JD & MG, Executive Director and Chairman of the Board of Directors of the Managing company KD Investments and the investment company KD Pelican, Executive Director of Capital Dynamics-Bulgaria and Euro-Phoenix Financial Advisors, and Vice Chairman of FSC. He has knowledge of English, German, Russian and Dutch language.

Andon Georgiev – Member of the Board of Directors and Procurator

In the calendar year 2018, part of management were also:

- Samuil Pavlov Shiderov – until 07 February 2018
- Alexander Angelov Georgiev – until 06 June 2018.

The company is represented by either two of the members of the Board of Directors, jointly, or by the Procurator and either one of the members of the Board of Directors, jointly.

The members of the BD of NGF EAD do not hold any shares of the Fund, nor do they have any special rights on the acquisition of such shares.

There are no contracts signed pursuant to Art. 240b of the Companies Act between the members of the BD of NGF EAD or persons related to them, on one hand, and the Company on the other, which fall outside the scope of the company's ordinary activity, or which significantly deviate from market conditions.

The participations, pursuant to Art. 247, Para. 2, item 4 of the Companies Act, of members of the SB and MB in commercial companies as general partners holding more than 25 per cent of the capital of another company, as well as their participation in the management of other business companies or cooperatives as procurators, managers or members of boards, is as follows (as of 31 December 2018) :

Stoyan Todorov Mavrodiiev – Chairman of the BD of NGF; he participates in the management of the following commercial companies:

- Chief Executive Director and Chairman of the MB of Bulgarian Development Bank AD, UIC 121856059
- Executive Director and Chairman of the Board of Directors Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank;
- sole equity owner of REAL ESTATE VENTURES EOOD, UIC: 131160908.

Angel Atanasov Djalazov – Vice Chairman of BD and Executive Director of NG; he participates in the following commercial companies:

- Micro Financing Institution Jobs, UIC: 201390740, member of BD and Executive Director;

– BG LIFE OOD, UIC: 175273067 – a partner holding a 25% share

Andon Georgiev Georgiev has no participation in the management or capital of other commercial companies.

Micro Financing Institution Jobs (MFI) EAD

MFI Jobs EAD also has a one-tier management system – Board of Directors (BD), which comprises from three to five members. The composition of BD at the end of 2018 was as follows:

Board of Directors:

Rumen Mitrov – Chairman of the Board of Directors

Nikolay Dimitrov – Vice Chairman of the Board of Directors

Angel Djalazov – Member of the Board of Directors and Executive Director

Hristina Todorova – Member of the Board of Directors and Procurator

Hristina Todorova holds a Master degree in Law from the University of National and World Economy. She has long-standing experience in the financial sector. She participated in the elaboration of many draft laws, practices and administrative procedures in the area of non-banking sector. For 10 years she has worked in the Financial Supervision Commission (FSC) at various expert and managerial positions. She occupied the positions of Head of the Judicial Protection Department and Director of the Legal Department of FSC. As Director of the Legal Directorate, Hristina Todorova leads both the activities of creating and developing the legal framework in the non-banking financial sector, the procedural representation of the FSC and its bodies, and the protection of the interests of financial service users. In 2016, Hristina Todorova was elected Chair of the newly established Sectoral Conciliation Commission on Consumer Disputes Hearing and Settlement in the area of insurance and insurance intermediation at the Commission for Consumer Protection, including upon provision of remote financial services to this sector. In 2017, Hristina Todorova was Director of the Legal Department at the Ministry of Health.

In the calendar year 2018, part of management was also:

Kostadin Bozhikov Munev – until 07 February 2018.

The company is represented by either two of the members of the Board of Directors, jointly.

There are no contracts signed pursuant to Art. 240b of the Companies Act between the members of the BoD or persons related to them, on one hand, and the Company on the other, which to fall outside the scope of the company's normal activity, or which significantly deviate from market conditions.

The participations, pursuant to Art. 247, Para. 2, item 4 of the Companies Act, of the members of the MB of Micro Financing Institution Jobs EAD in commercial companies as general partners holding more than 25 per cent of the capital of another company, as well as their participation in the management of other business companies or cooperatives as procurators, managers or members of boards, is as follows:

Rumen Mitrov – Chairman of the Board of Directors; he participates in the management of:

- Bulgarian Development Bank AD, UIC: 121856059, as Vice Chairman of the MB and Executive Director;
- Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank, as Vice Chairman of the Board of Directors.

Nikolay Dimitrov – Vice Chairman of the Board of Directors; he participates in the management of:

- Bulgarian Development Bank AD, UIC: 121856059, member of the MB and Executive Director;
- Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank, as a member of the Board of Directors

Angel Djalazov – Member of Board of Directors and Executive Director of the company; he participates in the management of:

- National Guarantee Fund, UIC: 200321435, Vice Chairman of the Board of Directors of the company and Executive Director.
- BG LIFE OOD, UIC: 175273067, a partner holding a 25% shareholding.

Hristina Todorova – member of the Board of Directors and Procurator; she does not participate in the management or capital of other commercial companies.

Capital Investment Fund (CIF) AD

BDB holds a share of 84.62% of the capital of Capital Investments Fund AD, UIC: 205322014, with the remaining 15.38 % of the capital of the company being subscribed by National Guarantee Fund AD.

CIF AD also has a one-tier management system – Board of Directors, comprising three members. At the end of 2018, the composition of BD was as follows:

Board of Directors:

Stoyan Mavrodiev – *Chairman of the Board of Directors and Executive Director*

Rumen Mitrov – *Vice Chairman of the Board of Directors*

Nikolay Dimitrov – *Member of the Board of Directors*

The company is represented by either two of the members of the Board of Directors.

There are no contracts signed pursuant to Art. 240b of the Companies Act between the members of the BD and/or persons related to them, on one hand, and the Company on the other, which fall outside the scope of the company's ordinary activity, or which significantly deviate from market conditions.

The participations, pursuant to Art. 247, Para. 2, item 4 of the Companies Act, of members of the BD of Capital Investments Fund AD in commercial companies as general partners holding more than 25 per cent of the capital of another company, as well as their participation in the management of other business companies or cooperatives as procurators, managers or members of boards, is as follows (as of 31 December 2018) :

Stoyan Mavrodiev – Chairman of the Board of Directors and Executive Director of the company; he participates in the management of the following companies:

- Bulgarian Development Bank AD, UIC: 121856059, Chairman of the MB and Chief Executive Director;
- National Guarantee Fund, EAD, UIC: 200321435, a subsidiary of the Bank, as Chairman of the Board of Directors;
- REAL ESTATE VENTURES EOOD, UIC: 131160908 – a sole equity owner;

Rumen Mitrov – Vice Chairman of the Board of Directors, ; he participates in the management of:

- Bulgarian Development Bank AD, UIC: 121856059, as Vice Chairman of the MB and Executive Director;
- Micro Financing Institution Jobs EAD, UIC: 201390740, a subsidiary of the Bank, Chairman of the Board of Directors.

Nikolay Dimitrov – Member of Board of Directors of the company, he participates in the management of:

- Bulgarian Development Bank AD, as a member of the MB and Executive Director;
- Micro Financing Institution Jobs EAD, UIC: 201390740, a subsidiary of the Bank, as a member of Board of Directors.

CIF was not operational as at 31 December 2018 and therefore, the it had no employees neither had it generated income.

Transactions with companies under joint control of the state

the owner of BDB is the Bulgarian state. Transactions with related parties and companies under the common control with the state are disclosed in Note 38 to the consolidated financial statements of BDB for 2018.

Events after the date of the financial statements

In pursuance of its strategy and designation of specific and new activities in separate companies, BDB incorporated two new subsidiaries – both with one single shareholder and 100 percent owned by the Bank – BDB Leasing EAD and BDB Factoring EAD. The companies were incorporated by decision of the MB dated 06 March 2019.

In April 2019, Fitch Ratings Agency upgraded the outlook of the long-term credit rating of Bulgarian Development Bank from BBB Stable Outlook to BBB, Positive Outlook.

Regarding the companies from the BDB Financial Group, there were no other significant events, which had occurred in the period from the reporting date to the date of approval of this report, which would require additional disclosures in the annual financial statements for the year ended 31 December 2018.

Management`s representations

Management of BDB declares that the enclosed annual consolidated financial statements give true and fair view of the property and financial position of the Bank at the end of 2018, and the determination of the financial result for the year in compliance with the applicable legislation. Suitable accounting policies have been used and applied consistently. In the preparation of the annual financial statements, judgments have been made, as necessary, in accordance with the prudence concept. Management applies consistently the applicable accounting standards and the annual financial statements have been prepared on a going concern basis.

The Bank's management dedicates efforts to maintain an adequate accounting system that complies with applicable accounting standards. The annual consolidated financial statements disclose the standing of the Bank with a reasonable degree of accuracy.

All measures have been undertaken to preserve the assets of the Bank, to prevent fraud and violations of the laws in the country and regulations of BNB on the bank activity.

The current Activity Report was approved on 10 July 2019 by MB of the Bulgarian Development Bank, and it was signed by:

EXECUTIVE DIRECTORS:



RUMEN MITROV

NIKOLAY DIMITROV

APPENDIX 1:

Corporate governance statement of BDB GROUP

This Corporate Governance Statement has been prepared on the grounds of Article 40, paragraph 1 of the Accountancy Act. The information provided takes into account the fact that Bulgarian Development Bank AD has not issued securities admitted to trading on a regulated market or shares traded on a multilateral trading facility.

BDB Group

At the end of 2018, the Financial Group Bulgarian Development Bank (the „Group“³ of the Financial Group) comprise Bulgarian Development Bank AD („BDB“, the „Bank“) and its subsidiaries – National Guarantee Fund EAD (NGF), Micro Financing Institution Jobs EAD (MFI Jobs) and Capital Investments Fund AD (CIF).

At the beginning of 2019, the Bank incorporated two new subsidiaries – BDB Leasing EAD and BDB Factoring EAD, which will become members of the Financial Group of BDB as well.

Being a financial institution established pursuant to a special act – the BDB Act („BDBA“) – and at the same time, applying all regulatory requirements of BNB and the European legislation, and in performing its mission of being a sustainable instrument of the government policy for promoting the development of the small and medium-sized businesses in Bulgaria, Bulgarian Development Bank AD has set as its goal to be a benchmark for good corporate governance and corporate responsibility while consistently and strictly observing the National Corporate Governance Code of 2016, The Code of Professional Conduct of 2017 adopted by the bank, the Code of Ethics of the Internal Audit of the BDB Group of 2015, as well as good corporate and banking practices.

Bulgarian Development Bank AD holds a license for an investment intermediary according to which it may provide investment services and perform investment activities under Article 6, paragraph 2 of the Markets in Financial Instruments Act (MFIsA), as well as additional services under Art. 6, paragraph 3 of the MFIsA.

Bulgarian Development Bank AD holds a license for an investment intermediary according to which it may provide investment services and perform investment activities under Article 6, paragraph 2 of the Markets in Financial Instruments Act (MFIsA), as well as additional services under Art. 6, paragraph 3 of the MFIsA. Investment services are provided and investment activities are performed in accordance with the requirements of MFIsA, Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (Directive 2014/65/EU or MIFID II), Regulation (EU) 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012 (Regulation (EU) 600/2014), Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive (Delegated Regulation (EU) 2017/565) and the acts on their implementation.

The Bank does not provide investments services, or perform investment activities under Article 6, paragraph 2, items 8 and 9 of the MFIsA – organisation of a multilateral trading facility and an organised trading facility.

Bulgarian Development Bank AD applies and maintains systems and producers that guarantee the security, completeness and confidentiality of its operations as an investment broker.

³ At the end of 2018, the Bank was a sole owner of the capital of TP Maritsa EOOD (TPM); however, the company was not a part of the strategic business model of the Financial Group of BDB.

In view of the above, the Bank has adopted and updated its internal regulations in accordance with the applicable legislation.

Bulgarian Development Bank AD

Bulgarian Development Bank AD (BDB, the Bank) was incorporated on 11 March 1999 as a joint stock company under the name of Encouragement Bank AD.

On 23 April 2018, the Bulgarian Development Bank Act (BDBA) was adopted. It arranges the scope of activity of the Bank and its subsidiaries that may be established.

The seat of Bulgarian Development Bank AD is Sofia 1000, Sredets area, 1 Dyakon Ignatii St.

As of 31 December 2018, Bulgarian Development Bank AD had no branches.

The Bank has fulfilled the requirements of BNB of minimum statutory shareholding capital for exercising bank activity, as well as the capital requirements of BDBA. Since its establishment and until August 2017, the government shareholding in BDB is controlled by the Ministry of Finance of the Republic of Bulgaria. On 04 August 2017, by amendment of the BDB Act pursuant to SG, issue 63 of 2017, the government shareholding went under the control of the Minister of the Economy of the Republic of Bulgaria. As of the date of preparation of this Statement, the ownership of the capital is allocated as follows: 99.9999% is owned by the Republic of Bulgaria, represented by the Ministry of the Economy, 0.0001% is owned by DSK Bank.

The capital of the parent company (the Bank) consists of 6,017,735 common, registered voting shares of par value BGN 100 each. The shares of BDB are not offered on a regulated market.

The Bulgarian Development Bank Act sets forth that a package of at least 51% of the shares of the capital of the Bank shall be state owned, where the shares of the State in the amount of no less than 51% of the subscribed shareholding capital shall be non-transferable. Furthermore, a specific restriction was established regarding the composition of the remaining shareholders, other than the Bulgarian state. The shares of the Bank cannot be pledged, and the rights attached thereto cannot be subject to transfer agreements.

Regarding the acquisition of its own shares, pursuant to Arts. 187e and 247 of the Companies Act, BDB declares that such an acquisition has not taken place, as well as that there are no shares or bonds of the company acquired, held or assigned by the Board Members of the during the reported year.

Pursuant to Art. 6 Par. 4 of the BDB Act the shares in the capital of the Bank, besides the Bulgarian state, may be acquired and owned by the Council of Europe Development Bank, the European Investment Bank and the European Investment Fund, by development banks of Member States of European Union. In these cases art. 31 of the Credit Institutions Act does not apply.

Pursuant to Art. 6 Par. 4 of the BDB Act the members of the Management and controlling bodies, the procurators and the senior management cannot hold shares and cannot be provided with options for shares of BDB, and in subsequent accounting periods no agreements may be concluded as a result of which in any future period changes may occur the relative volume of shares held by current shareholders.

The management of BDB is carried out in compliance with Art. 5 of the BDB Act, pursuant to which the Bank has a two-tier system of governance and the rights of the state during the General assembly of shareholders of the Bank are exercised by the Minister of the Economy. Outside the powers of the Minister of the Economy, any amendment to the BDB Act and the right to issue or buy back shares are only possible by voting a new act or by amending the current act by the National Assembly. Under this article, only the Minister of the Economy, acting as representative of the majority shareholder in BDB, may decide to reduce the share capital through the redemption of shares.

At the end of 2018, BDB had not liabilities under existing or new issues of securities.

As of 31 December 2018, there is no pending court, administrative or arbitration proceeding related to liabilities or receivables of the BDB Group, amounting to 10 per cent or more from its equity.

Pursuant to the Statute of BDB, the lending activity of the Bank is focused on:

- Pre-export and export financing of small and medium-sized enterprises (SMEs),
- Financing other operations of SMEs, either through intermediary banks or directly,
- Refinancing of banks granting loans to SMEs,
- Financing of investments by SMEs abroad,
- Participation in public and public-private projects or partnerships of strategic, national or regional importance.

The Bank extends also other types of loans according to a procedure set by the Management Board, whereas the amount of the exposure to one customer or a group of related customers is subject to the requirements and limitations laid down in Regulation 575/2013/EU.

The Bank shall not lend funds to:

1. Activities not compliant with the National law, including for environment protection;
2. Business companies with unknown ultimate controlling owner;
3. Political parties and persons related to them. Persons related to political parties may be: youth, women.s and other organizations, which the parties may establish according to law, as well as entities, established by the political parties for performing the only business activities, which they are legally allowed to do – publishing activity, copyrights and using intellectual property, as well as the sale and distribution of printed, audio and audio-visual materials with party campaigning content;
4. Non-profit enterprises and organizations;
5. Media;
6. Activities related to sport and sports initiatives;
7. Activities prohibited by law.

The Bank provides loans directly or through commercial banks – intermediaries.

The terms and conditions for providing loans are determined by the Management Board.

The Management Board passes unanimous decision to form exposures to one client or a group of related clients, if it exceeds 5% of the Bank.s equity, in compliance with requirements of the Credit Institutions Act and the internal rules of the Bank.

In view with its specific function related to carrying out state policy on promoting the business, BDB prioritizes its activity programs and products to promote SMEs, on-lending programs, export financing and financing under assigned mandates. The biggest credit exposure of the Bank, provided to a group of related parties /other than bank institutions/, amounts to BGN 150,129 thousand according at amortized cost (2017: BGN 69 259 thousand.), which represents 23.22% of the Bank's equity (2017: 10.88%) (the eligible capital of the Bank calculated in accordance with Regulation 575 /2013/EU is equal to BGN 646,679 thousand (2017: BGN 636,570 thousand)). Analysis of the structure of the credit portfolio by segments is provided in the consolidated financial statements.

Bearing in mind the specific activity of the Bank, as of 31 December 2018, the funds attracted from 20 largest non-bank depositors represent 95.26% of the total amount of liabilities to other clients (31 December 2017: 97.13%).

In view of its specific activity, the BDB Group utilizes significant external funding from international financial institutions. Detailed information on the received external credit lines is disclosed in a separate Note to the Financial Statements.

National Guarantee Fund EAD (NGF)

National Guarantee Fund EAD (NGF) is a company founded on 12 August 2008 on the basis of the Bulgarian Development Bank Act (BDBA) and was registered at the Commercial Registry on 22 August 2008. According to the Credit Institutions Act (CIA), the National Guarantee Fund EAD is a financial institution entered in 2009 into the Registry by BNB under Art.3, Par.2 of the Credit Institutions Act (CIA). In compliance with the Statute of the company the scope of activity is:

- Issuing guarantees for supplementing the collateral under loans to small and medium-sized enterprises;
- Offering other products to small and medium-sized enterprises, like: guarantee for participation in a tender; performance guarantee; advance payment guarantee; guarantee for payment of a loan of an exporter, etc;
- Issuing guarantees for supplementing collateral under loans to small and medium-sized enterprises, carrying out research and development and for implementing these products and scientific developments into the industry;
- The guarantees issued by NGF at its own risk may cover not more than 50 percent of the liability. By an amendment to the BDB Act, promulgated in the State Gazette, issue 102 of 21 December 2012, the guarantees issued by NGF EAD in connection with guarantee schemes under the Rural Development Programme 2007 – 2013 and Operational Programme Fisheries Sector Development 2007 – 2013 may cover up to 80 percent of the liability;
- Other activities, not particularly prohibited by law.

The registered capital of the company as of 31 December 2018 amounted to BGN 80,000,000 split into 800,000 shares with nominal amount of BGN 100 each, the shares are ordinary, materialised, registered and indivisible, and each share gives the right to one vote. The company's capital is fully paid-in.

The seat and registered address of the National Guarantee Fund EAD (NGF) is Sofia, 1 Dyakon Ignatii St.

As of 31 December 2018, NGF had no branches.

Micro Financing Institution Jobs EAD (MFI Jobs)

Micro Financing Institution JOBS EAD (MFI Jobs) was recorded into the Commercial Registry on 14 January 2011. The scope of activity is micro-financing, including providing micro-loans, acquiring from third parties and leasing industrial equipment, automobiles and other vehicles, as well as other items /finance lease/, purchase and sale, and import of such items, consulting services, trade representation and mediation for local and foreign physical and legal bodies performing their activity in the country, as well as any other activity not forbidden by law.

The registered capital of MFI Jobs as of 31 December 2018 amounted to BGN 7,643,000 split into 76,430 shares with nominal amount of BGN 100 each, the shares are ordinary, materialised, registered and indivisible, and each share gives the right to one vote. The company's capital is fully paid-in.

The seat and registered address of Micro Financing Institution Jobs EAD is Sofia, 1 Dyakon Ignatii Str.

As of 31 December 2018, MFI JOBS had no registered branches.

Capital Investments Fund AD (CIF AD)

Capital Investments Fund EAD (CIF) was incorporated on 24 August 2018 and registered on 04 October 2018 as a joint-stock company with 100 percent of ultimate participation of BDB (84.62% of direct participation of BDB, or 550,000 shares, and indirect participation through NGF – 15.38%, the owner of the remaining 100,000 shares). The registered address of MFI is at 1 Dyakon Ignatii Str., Sofia. The registered capital of as of 31 December 2018 consisted of 650,000 registered shares with nominal amount of BGN 100, including paid-in capital as of 31 December 2018 of BGN 16,250,000.

The object of activity of CIF includes:

- Participation in the capital of small and medium-sized enterprises;
- Provision of consulting services regarding the capital structure of small and medium-sized enterprises; advice and services on incorporation of entities under Article 261 of the Commercial Act;
- Investment consultancy;
- Consulting services on the management of pools of securities of small and medium-sized enterprises;
- Other activities, not particularly prohibited by law.

As of 31 December 2018, CIF had no registered branches and did not carry out operating activities.

Risk management within the Group of BDB

In the course of their ordinary activity, the companies from the BDB Group are exposed to various risks, the occurrence of which may lead to losses and to deterioration of the financial stability of the Group. These risks are identified, measured and assessed using controlling mechanisms in order to be managed and to avoid any unjustified concentration of a particular risk. The risk management process is important for profitability and for its existence. The most significant risks, to which the Group is exposed, are credit, market and operational risks.

In managing the various types of risk arising out of the activity, the Group follows the principles of conservatism, objectivity and full compliance with all applicable national and European legislative acts and regulatory recommendations. In support of this policy, the Group maintains substantially higher levels of liquid buffers and capital adequacy than the statutorily required.

Credit Risks to which BDB Group is exposed

The credit risk is the main risk, to which BDB and the Group companies are exposed, therefore its management is crucial for its activity. The credit risk management takes place in compliance with the BDB Act and the effective laws and regulations of the Republic of Bulgaria that regulate the credit activity and the approved international standards and established best banking practices.

BDB uses an internal rating model for the assessment and management of the credit risk (incl. from counterparties) under the exposures. Bodies for monitoring, control and assessment of the quality of the credit portfolio have been created and are functioning in BDB. Procedures and mechanisms have been introduced for ongoing monitoring, recording and management of the credit portfolio requiring periodic and, if necessary, extraordinary reports on the financial and legal status of each borrower and liable persons. If new circumstances are established, which may lead to a change to the risk profile of the borrowers, including increasing the risk of default of the credit exposure, adequate and conforming measures risk profile of the debtor, are undertaken.

In managing the credit risk BDB applies a system of internal limits, determined by in-house regulations of the Bank, on a consolidated basis by economic sectors, by instruments, as well as other credit restrictions and

limits on concentration, while the results from the monitoring of their compliance are reported to the competent bodies. The system of limits is reviewed and updated periodically.

The credit risk management of the commitments recoded off-balance sheet (guarantees) of NGF takes place at two levels – at the level of the individual deal (guarantee) and at portfolio level. The credit risk at individual level is managed according to the internal rules and procedures for guarantee activity where the proposal for issuing a guarantee (undertaking a guarantee commitment) is reviewed and approved by the risk manager of NGF, then it is handed over for approval by two of the members of the Board of Directors of NGF. After having collected all approvals, the confirmation for issuing the guarantee is signed by the representatives of NGF. Under the guarantee scheme under the Rural Development Program there is a second level of approval – the so called Advisory Committee comprised of representatives of the Ministry of Agriculture and Foods and BDB, which approves each undertaken guarantee commitment under the program. At portfolio level, the credit risk is managed by set up limits for payment (caps), limiting the commitment of NGF to paying to a given bank up to a certain share of the size of the portfolio of guarantees issued under a specific program. The subsequent management of the credit risk assumed by NGF is through monitoring procedures, within which the Fund may exclude from coverage certain loans, which do not correspond to specific requirements of the signed guarantee agreements, from the guaranteed portfolio.

The policy, which MFI JOBS has adopted in order to minimize the credit risk, is to make a preliminary assessment of the creditworthiness of the clients, as well as to request additional collateral under the lease and loan contracts and the transferred entitlements – insurances of lease assets, registration of the lease contracts in the Central Registrar of Special Pledges (CRSP), suretyships, promissory notes and special pledges on receivables, as well as mortgage of real estate and/or pledge on movable property when granting the loan.

In 2018, the subsidiary of the Bank – Capital Investments Fund AD, was not operational.

Market risks to which BDB Group is exposed

In managing the currency risk, BDB and the Group follow the principle of maintaining minimum open FX positions through the observing of established limits. The positions in various currencies, as well as the general FX position, are monitored on a daily basis. The FX positions are not formed for speculative purposes, but are the consequence of the currency transactions, occurring in the course of the ordinary bank activity. In managing its assets and liabilities, due to the specifics of its financing, BDB seeks to maintain these assets and liabilities in EUR or BGN. The Bank's open FX position takes into account the terms and possibilities for netting the EUR and BGN positions in accordance with the applicable regulatory framework.

Regular reports, distributed periodically according to their sensitivity to changes in the interest rates, are prepared on the financial assets and liabilities in order to manage the interest risk. A system of limits was introduced in connection with the fluctuations in the interest curve, while stress scenarios are applied to the discrepancies by periods, thus estimating the potential risk for the interest revenues and the capital of the Bank and the Group.

The assumption of risks when transacting on the money and capital markets is managed by a system of limits reflecting the risk profile of the investments. These limits are determined according to parameters of the portfolio, like counterparty, financial instrument, maturity, etc. The system of limits is periodically reviewed, while the compliance with the limits is subject to daily monitoring. The securities portfolio, created by the BDB Group in order to invest the available funds, is characterized by a relatively low interest rate risk and comprises relatively liquid government securities and securities issued by reliable institutions, i.e. low price risk. Due to the absence of a trade portfolio pursuant to the statutory regulations, the BDB Group does not allocate capital for market risk.

The liquidity of the Bank is managed by strictly monitoring the ratios, indicating the liquidity position by periods. The liquidity risk is measured by applying additional scenarios for the cash flows from operations. In addition, the liquid buffers of the Bank are measured and monitored, as well as the additional sources of financing upon market and idiosyncratic shocks. The observing of the limits for liquidity ratios is monitored and reported regularly before the competent authorities.

Operational risk to which BDB Group is exposed

The operational risk is managed by strictly monitoring and registering all operational events occurring in the activity of the various units as a result of the processes within the Group. Operational events, which are more frequent, and the ones having great potential or real impact on the financial result of BDB and the Group companies, are subject to strict investigation and monitoring. They serve as the basis for the analysis of the operational risk in various scenarios, including operational risk stress tests. The operational risk is measurable and controllable, while a registry of the operational events is maintained and used as basis for analysis and improvement of the bank's working processes and for minimizing the conditions, which could potentially lead to operational events and loss for the Group. The necessary capital for operational risk is calculated by using the basis indicator approach pursuant to the applicable regulatory framework.

Structure of risk management

The main units directly responsible for risk management, are the follow:

For the Parent Company (the Bank):

- Supervisory Board – performs overall supervision on risk management;
- Audit committee to the Supervisory Board – implements best practices of independent audit control and the establishment of system of the three pillars for control in the financial sectors according to the recommendations from Basel III;
- Internal audit – provides assurance to the Bank's top management on risk management effectiveness, internal control and management;
- Management Board – it is responsible for overall risk management approach and for approval of risk strategies, principles and the specific methods, techniques and procedures;
- Risk Committee – it is responsible for the control on the implementation of the management policies of various types of risk and the adequacy of the risk profile of the Bank to the assigned tasks to it;
- Committee of Assets and Liabilities Management (ALCO) – it is responsible for the strategic management of the assets and liabilities, and for the management of the market risks, incl. liquidity risk, related to assets and liabilities;
- Committee on Remunerations and Committee on Recruitment – responsible for the management of activities in the field of human resources.
- Executive Directors and Members of the MB – exercise current operating control on maintaining and observing the specified limits for the particular types of risk and the application of the established procedures;
- Risk Management Department – develops and implements the risk management system. The Department prepares and submits periodic reports to the Board of Directors in order to evaluate the risks in the business activity, incl. the keeping within the limits, and it regularly reports to the operational management of the Company. It performs initial and ongoing inspection of the risk assessment methods. It controls the input data necessary for evaluating the risk according to an applicable method of reliability and sufficiency.
- Compliance Department – monitors and ensures compliance with policies, processes and procedures within the Bank. The Department reports to the MB, on a regular basis, on all compliance matters – establishment and taking measures for remedy of any inconsistencies that might have been found;

- Planning, Analysis and Regulations Department – submits reports to the MB and BNB, reports on key indicators, business plans and their performance, and identifies any risks at operational, business, reporting and strategic level, and interacts with the other units of the Bank for the purpose of their management;
- The Central Bank performs supplementary supervision on the risk management in the Bank by requesting periodic regulatory reports and subsequent control on the compliance with statutory maximum levels of exposure of the Bank to particular risks.

For the subsidiary National Guarantee Fund (the Fund):

The main units directly responsible for risk management are the following:

- Management Board of BDB AD (the parent company) – performs overall supervision on risk management;
- Board of Directors – carries out overall risk management supervision; responsible for overall risk management approach and for approval of risk management strategies, principles and the specific methods, techniques and procedures;
- Committee on Provisions – analyses the guaranteed portfolios in terms of overall credit risk management for the total guaranteed portfolio, as well as of each guarantee deal and beneficiary of the guarantee itself.
- Risk and Monitoring Department – performs general monitoring with respect to the guaranteed portfolios by carrying out inspections (current and after a claim for payment has been filed) of the commercial banks regarding the fulfilment of the terms and conditions of their guarantee agreements at the level of both the separate client and individual portfolio. The Department also identifies, assesses, monitors and applies measures for limiting the impact of the major risks.

For the subsidiary Micro Financing Institution JOBS EAD (MFI):

The main units directly responsible for risk management are:

- Board of Directors – adopts rules and procedures for risk management. Controls risk factors for the activity of the Company and adopts resolutions within its powers. It also analyses the credit transactions amounting to above BGN 100,000 in terms credit risk management;
- Credit Committee – it continuously monitors and analyses the credit and lease portfolio of the Company from the point of view of the credit risk, incl. on the level of individual transaction;
- Credit Council – analyses the credit and lease deals from the point of view of credit risk management during their authorization and/or renegotiation;
- Operational management (Executive Director and Procurator) – organizes the activities for implementation of the Rules on Risk Management adopted by the Board of Directors. Creates a work organization, which ensures the observation of the specified limits and levels of risk. Exercises control over the compliance of the analysis, risk estimation and evaluation procedures used by the relevant employees with the internal legislative documents adopted by the Board of Directors;
- Risk Management Department – develops and implements the risk management system. Prepares and submits periodic reports to the Board of Directors in order to evaluate the risks in the business activity, incl. the keeping within the limits, and it regularly reports to the operational management of the Company. It performs initial and ongoing inspection of the risk assessment methods. It controls the input data necessary for evaluating the risk according to an applicable method of reliability and sufficiency.

Bank supervision authorities pursuant to the Bulgarian legislation

In compliance with the requirements of the framework of the laws and by-laws regulating the banking activity in the country, BDB must follow limitations, related to certain ratios in its separate and consolidated financial statements. As of 31 December 2018, BDB has observed all regulatory requirements of BNB and the Bulgarian legislation. The amounts of key ratios – capital adequacy and asset coverage ratio – are among the highest within the Bulgarian banking system.

Control environment

BDB follows a management philosophy and operating style subordinate to the principles of conservatism when performing the strategic goals of the Bank assigned pursuant to the BDB Act.

The Bank applies the model of the three lines of defence within the risk management:

The first line of defence is the management control that the leaders of the operational units are exercising. The operational management identifies, evaluates, controls and mitigates risks, ensuring that they operate in accordance with the objectives set out in advance.

The second line of defence is the risk management and compliance function carried out by the Risk Management, Compliance and the Classified Information Departments with regard to the prevention of money laundering and terrorist financing. In their activities, these departments are supported by Management, Analysis and Regulation and Legal Departments. The second line of defence is independent from the first one in terms of organisation, and carries out preventive and ongoing control.

The third line of defence is the internal control function. Internal Audit of the Group Department carries out ex-post control and provides assurance to senior management with respect to the effectiveness of risk management, internal control and corporate governance, as well as the way in which the first and second lines achieve the risk management and control objectives. Internal Audit of the Group Department provides comprehensive assurance from the position of the highest level of independence in the organisation, through a direct subordination to the Supervisory Board (SB).

Management assigns powers and responsibilities for the operating activity in line with a detailed internal normative set of documents, which are in conformity with the current national and European legislations, where in order to guarantee the relationships in accountancy and reporting, and various specialized committees, by hierarchy of authorities, were formed to the MB and SB of BDB.

The Bank has developed an internal set of documents, which includes policy and communications focused on ensuring that all employees understand the goals of the Bank, knows how individual actions are interconnected and contribute towards these goals, and who and how is reporting and what is their responsibility.

The Bank has established an information system, including business processes related to it, providing the necessary quality and control of the financial accountability and communication.

The Bank's Audit Committee monitors the financial reporting processes, the effectiveness of internal control systems and the effectiveness of risk management systems; moreover, it monitors the independent financial audit, conducts a review of the independence of the registered auditor, and makes recommendations for selecting a registered auditor.

Corporate governance of Bulgarian Development Bank

Bulgarian Development Bank AD has a two-tier corporate governance structure, which consists of Supervisory Board (SB) and Management Board (MB).

As of 31 December 2018, the structure of the management bodies has the following components:

Supervisory Board of BDB:
***Luchezar Borisov* – Chairman of the SB**

Luchezar Borisov was born in 1978 in Samokov. He completed his Master studies in Macroeconomics and Accounting and Finance at the University of National and World Economy (UNWE). He has several specializations in Bulgaria and abroad, including in Entrepreneurship and Risk Capital in AUBG, Project Management in WIFI, Austria, Encouragement of Foreign Direct Investments in JICA, Japan, Stock-exchange and Banking in CITIBANK, etc. He has rich experience in corporative management. Mr. Borisov has been part of the management of both private and state-owned companies in the Industry, energy and financial sectors. Currently he is a Deputy Minister of Economy.

***Mitko Simeonov* – Deputy Chairman of the SB**

Mitko Simeonov has a Master degree in Law from the New Bulgarian University and a Master degree in International Economic Relations from the University of National and World Economy. He also holds a postgraduate degree in financial management from the University of National and World Economy. He was Deputy Executive and Executive Director of the Agency for Privatization and Post-Privatization Control.

***Velina Burska* – Member of the SB**

Velina Burska has a Master Degree in Economics and Organization of Internal Trade from the University of National and World Economy. From 2002 to 2017 she was the director of the Post-Privatization Control Directorate at the Agency for Privatization and Post-Privatization Control.

In fulfilment of the good practices of control and the system of the three pillars recommended within Basel III, a specialized body made up of Audit Committee, Risk Committee, Remunerations Committee and Recruitment Committee functions to the Supervisory Body.

Member	Risk Committee	Recruitment Committee	Remunerations Committee
Luchezar Borisov	Chairman	Chairman	Chairman
Mitko Simeonov	Member	Member	Member
Velina Burska	Member	Member	Member

Audit Committee:

Mrs Svetla Lambreva – Chair of the Audit Committee

Mrs Rositsa Grigorova – Member of the Audit Committee;

Mrs Kalina Mavrova – Member of the Audit Committee.

Management Board of BDB:

Stoyan Mavrodiiev – Chairman of the Management Board and Chief Executive Director

Stoyan Mavrodiiev holds a Master degree in Law from Sofia University “St. Kliment Ohridski” and a Master degree in Finance from the University of National and World Economy. He attended a series of courses at the International Tax Academy in Amsterdam, and has also trained in the US Department of State’s International Program of Leaders. His career started as a legal, tax and business consultant at PriceWaterhouseCoopers. In the period 1996-2006, he worked as a financial and legal consultant in the United Consulting, which he also managed. From 2009 to 2010 he is Deputy Chairman of the Commission for Economic Policy, Energy and Tourism and member of the Budget and Finance Committee of the 41st National Assembly. For 6 years (2010-2016), he is Chairman of the Financial Supervision Commission (FSC), which oversees and regulates the financial system and the non-banking financial sector in Bulgaria. From 2010 to 2016 he is a member of the Advisory

Financial Stability Board (FSF). In this period, it is also a member of a number of international organizations, including ESMA, EIOPA, ESRB, IOSCO, IAIS and IOPS.

Rumen Mitrov — Deputy Chairman of the Management Board and Executive Director

Rumen Mitrov holds a Master of Accounting and Control from the University of National and World Economy. His professional experience began in 1994 at NRA Sofia. In the period 2000-2003 he is the manager of the petroleum products import company “GMN GAZ”, and from 2003 to 2011 he is engaged in financial and tax consultancy as manager of the two accounting companies “Eurotim Bulgaria” and “RM Consult”. From 2011 to 2016, he was consecutively appointed Director of “Investment Activity Supervision”, “Regulatory Policy”, and “Coordination, Analysis and Policy of Supervisory and Supervision Activities” divisions in the Financial Supervision Commission (FSC).

Nikolay Dimitrov — Member of the Management Board and Executive Director

Nikolay Dimitrov holds a Ph.D. in Economics from the University of National and World Economy (UNWE) with specializations “International Economic Relations” and “Finance”. Between 2007 and 2015, he completed a number of additional courses and qualifications at the Judge Business School at Cambridge University (UK), the Investment Banking Institute (USA), among others. His banking career started at the end of 2003 and went through Raiffeisen Bank and United Bulgarian Bank. He joined the Bulgarian Development Bank in July 2011, in January 2012 become Head of the Investment Banking and Project Finance Department, and since April 2013 he is Head of the Corporate Banking Division. Alongside, he has been an associated professor at the Department of International Economic Relations at UNWE over the period 2010 – 2017.

Until 06 March 2018, Ilia Vasilev Kirchev was also a member of the Management Board of BDB.

Bulgarian Development Bank AD is represented by either two of the Chief Executive Directors, Executive Directors and the Procurator, jointly.

There were no charges in the main corporate governance principles of the BDB Group in 2018.

Committees of the Management Board

The BDB Management Board, in conformity to the current legislation in Bulgaria and in EU, and following the best banking practices, has delegated part of its authorities to specialized committees – Committee on Assets and Liabilities Management and Commission on Complaints and Signals.

Meetings of the Committee on Assets and Liabilities Management (ALCO) take place on a monthly basis, at which meetings the main indicators having relevance to the strategic management of the assets and liabilities of the bank are reviewed. The main functions of ALCO are to identify, manage and monitor the liquidity risk of the Bank, to determine the strategy for attracting resources, to determine the pricing policy for the loans in order to ensure adequate margin above the costs of funds, to decide on the strategic liquidity of the Bank in order to ensure a regular and timely settlement of the current and future liabilities, both during normal circumstances and in event of liquidity crisis, to determine the structure of the liquidity buffers and the sources of additional funding. The materials reviewed at the meetings of the ALCO, along with the minutes from them, are reported to the Management Board of BDB on a timely basis after each session. In addition to the board members, participants in these meetings are also the heads of key departments in the Bank.

	Committee on Assets and Liabilities Management (ALCO)	Commission on Complaints and Signals*
Stoyan Mavrodiev	Member	
Rumen Mitrov	Member	
Nikolay Dimitrov	Chairman	
Head of Risk Department	Member	Member
Head of Legal Department		Member
Head of Security Department		Member
Head of the Planning, Analysis and Regulations Department	Member	Member
Head of the Group Internal Audit Department		Member
Deputy Head of Treasury Department	Member	
Head of the Compliance Department		Chairman
Head of the International Financial Institutions and EU Funds Department	Member	

* The Chair of the Commission is elected by the members for a period of one year.

CONTRACTS WITH RELATED PARTIES INVOLVED IN THE MANAGEMENT AND PARTICIPATION OF MEMBERS OF THE MB AND SB OF THE BANK IN OTHER COMPANIES

There are no signed contracts pursuant to Art. 240b of the Companies Act between the members of the SB and MB or persons related to them, on one hand, and the Bank, on the other, which fall beyond the ordinary course of business or which significantly deviate from the market conditions.

In 2018, there were no concluded deals between BDB and its related parties, or offers for signing such deals, which fall outside the scope of the ordinary activity, or which significantly deviate from the market conditions, to which BDB or its subsidiary is a party.

There are no material contracts concluded, which lead to action, are amended, or terminated, due to change in the control of or over the Bank, or as a result of a compulsory public procurement procedure. As far as there is a legal restriction regarding the shareholding structure of BDB, pursuant to the BDB Act, no such contracts are expected to be concluded.

There is no practice of concluding agreements among the BDB Group companies and their management bodies and/or employees for the payment of compensation upon resignation or dismissal without legal grounds thereof, or upon terminating the legal employment relationships by reasons related to tender offers.

The participations, pursuant to Art. 247, Para. 2, item 4 of the Companies Act, of members of the SB and MB in commercial companies as general partners holding more than 25 per cent of the capital of another company, as well as their participation in the management of other business companies or cooperatives as procurators, managers or members of boards, is as follows (as of 31 December 2018):

- With respect to members of the SB of the Bank: **Luchezar Dimitrov Borisov** – Chairman of the SB – he participates in the management of Energy Efficiency and Renewable Sources Fund, UIC: 131330278, member of the MB of the company
- **Mitko Emilov Simeonov** – he has no participations in the capital and management of other companies
- **Velina Ilieva Burska** – she has no participations in the capital and management of other companies



With respect to members of the Management Board (MB):

Stoyan Todorov Mavrodiev – Chief Executive Director, Chairman of the MB; he participates in the management of the following commercial companies:

- Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank, as Chairman of the Board of Directors and Executive Director;
- NATIONAL GUARANTEE FUND EAD, UIC: 200321435, a subsidiary of the Bank, as Chairman of the Board of Directors;
- REAL ESTATE VENTURES EOOD, UIC: 131160908, a sole equity owner.

Rumen Dimitrov Mitrov – Executive Director, Vice Chairman of the MB, he participates in the management of the following commercial companies:

- Micro Financing Institution Jobs EAD, UIC 201390740, a subsidiary of the Bank, as Vice Chairman of the Board of Directors;
- Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank, as Vice Chairman of the Board of Directors;

Nikolay Dimitrov Dimitrov – Executive Director, member of the MB; he participates in the management of the following commercial companies:

- Micro Financing Institution Jobs EAD, UIC 201390740, a subsidiary of the Bank, as a member of the Board of Directors;
- Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank, as a member of the Board of Directors;

Information about the full amount of the compensations, rewards and/or benefits for the members of the Management and control bodies for the fiscal accounting year, paid by the issuer and its subsidiaries is disclosed in the notes to the financial statements.

Management of the subsidiaries

As of 31 December 2018, BDB is the equity owner of the following subsidiaries:

- The sole owner of:
 - National Guarantee Fund EAD, UIC: 200321435;
 - Micro Financing Institution Jobs EAD, UIC: 201390740;
 - Trade Centre Maritsa EOOD, UIC: 115619162
- Co-owner jointly with NGF of Capital Investments Fund AD, UIC: 205322014, with the following distribution of the subscribed (84.62% for BDB and the remaining 15.38% for NGF).

National Guarantee Fund

NGF EAD has a one-tier management system – Board of Directors, comprising three members. As of 31 December 2018, the composition of BD was as follows:

Board of Directors of the company:

Stoyan Mavrodiev – Chairman of the Board of Directors

Angel Djalazov – Vice Chairman of the Board of Directors and Executive Director

Angel Djalazov has over 15 years of experience in international investment banking, asset management, capital markets, project finance, investment products, supervision and financial instruments management. He has occupied consequently the positions of an investment manager of TBD Fund, Director of Legal Department at JD & MG, Executive Director and Chairman of the Board of Directors of the Managing company KD Investments and the investment company KD Pelican, Executive Director of Capital Dynamics-Bulgaria and Euro-Phoenix Financial Advisors, and Vice Chairman of FSC. He has knowledge of English, German, Russian and Dutch language.

Andon Georgiev Georgiev – Member of the Board of Directors and Procurator

In the calendar year 2018, part of management were also:

- Samuil Pavlov Shiderov – until 07 February 2018
- Alexander Angelov Georgiev – until 06 June 2018.

The company is represented by either two of the members of the Board of Directors, jointly, or by the Procurator and either one of the members of the Board of Directors, jointly.

The members of the BD of NGF EAD do not hold any shares of the Fund, nor do they have any special rights on the acquisition of such shares.

There are no contracts signed pursuant to Art. 240b of the Companies Act between the members of the BD of NGF EAD or persons related to them, on one hand, and the Company on the other, which fall outside the scope of the company's ordinary activity, or which significantly deviate from market conditions.

The participations, pursuant to Art. 247, Para. 2, item 4 of the Companies Act, of members of the SB and MB in commercial companies as general partners holding more than 25 per cent of the capital of another company, as well as their participation in the management of other business companies or cooperatives as procurators, managers or members of boards, is as follows (as of 31 December 2018) :

Stoyan Todorov Mavrodiiev – Chairman of the BD of NGF; he participates in the management of the following commercial companies:

- Chief Executive Director and Chairman of the MB of Bulgarian Development Bank AD, UIC 121856059
- Executive Director and Chairman of the Board of Directors Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank;
- sole equity owner of REAL ESTATE VENTURES EOOD, UIC: 131160908.

Angel Atanasov Djalazov – Vice Chairman of BD and Executive Director of NG; he participates in the following commercial companies:

- Micro Financing Institution Jobs , UIC: 201390740, member of BD and Executive Director;
- BG LIFE OOD, UIC: 175273067 – a partner holding a 25% share

Andon Georgiev Georgiev has no participation in the management or capital of other commercial companies.

Micro Financing Institution Jobs (MFI) EAD

MFI Jobs EAD also has a one-tier management system – Board of Directors (BD), which comprises from three to five members. The composition of BD at the end of 2018 was as follows:

Board of Directors:

Rumen Mitrov – Chairman of the Board of Directors

Nikolay Dimitrov – Vice Chairman of the Board of Directors

Angel Djalazov – Member of the Board of Directors and Executive Director

Hristina Todorova – Member of the Board of Directors and Procurator

Hristina Todorova holds a Master degree in Law from the University of National and World Economy. She has long-standing experience in the financial sector. She participated in the elaboration of many draft laws, practices and administrative procedures in the area of non-banking sector. For 10 years she has worked in the Financial Supervision Commission (FSC) at various expert and managerial positions. She occupied the positions of Head of the Judicial Protection Department and Director of the Legal Department of FSC. As Director of the Legal Directorate, Hristina Todorova leads both the activities of creating and developing the legal framework in the non-banking financial sector, the procedural representation of the FSC and its bodies, and the protection of the interests of financial service users. In 2016, Hristina Todorova was elected Chair of the newly established Sectoral Conciliation Commission on Consumer Disputes Hearing and Settlement in the area of insurance and insurance intermediation at the Commission for Consumer Protection, including upon provision of remote financial services to this sector. In 2017, Hristina Todorova was Director of the Legal Department at the Ministry of Health.

In the calendar year 2018, part of management was also:

Kostadin Bozhikov Munev – until 07 February 2018.

The company is represented by either two of the members of the Board of Directors, jointly.

There are no contracts signed pursuant to Art. 240b of the Companies Act between the members of the BoD or persons related to them, on one hand, and the Company on the other, which to fall outside the scope of the company's normal activity, or which significantly deviate from market conditions.

The participations, pursuant to Art. 247, Para. 2, item 4 of the Companies Act, of the members of the MB of Micro Financing Institution Jobs EAD in commercial companies as general partners holding more than 25 per cent of the capital of another company, as well as their participation in the management of other business companies or cooperatives as procurators, managers or members of boards, is as follows:

Rumen Mitrov – Chairman of the Board of Directors; he participates in the management of Bulgarian Development Bank AD, UIC: 121856059, as Vice Chairman of the MB and Executive Director;

– Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank, as Vice Chairman of the Board of Directors.

Nikolay Dimitrov – Vice Chairman of the Board of Directors; he participates in the management of:

– Bulgarian Development Bank AD, UIC: 121856059, member of the MB and Executive Director;

– Capital Investments Fund AD, UIC: 205322014, a subsidiary of the Bank, as a member of the Board of Directors

Angel Djalazov – Member of Board of Directors and Executive Director of the company; he participates in the management of:

– National Guarantee Fund, UIC: 200321435, Vice Chairman of the Board of Directors of the company and Executive Director.

– BG LIFE OOD, UIC: 175273067, a partner holding a 25% shareholding.

Hristina Todorova – member of the Board of Directors and Procurator; she does not participate in the management or capital of other commercial companies.

BDB holds a share of 84.62% of the capital of Capital Investments Fund AD, UIC: 205322014, with the remaining 15.38 % of the capital of the company being subscribed by National Guarantee Fund AD.

Capital Investments Fund (CIF) AD

CIF AD has a one-tier management system – Board of Directors, comprising three members. At the end of 2018, the composition of BD was as follows:

Board of Directors:

Stoyan Mavrodiev – *Chairman of the Board of Directors and Executive Director*

Rumen Mitrov – *Vice Chairman of the Board of Directors*

Nikolay Dimitrov – *Member of the Board of Directors*

The company is represented by either two of the members of the Board of Directors.

There are no contracts signed pursuant to Art. 240b of the Companies Act between the members of the BD and/or persons related to them, on one hand, and the Company on the other, which fall outside the scope of the company's ordinary activity, or which significantly deviate from market conditions.

The participations, pursuant to Art. 247, Para. 2, item 4 of the Companies Act, of members of the BD of Capital Investments Fund AD in commercial companies as general partners holding more than 25 per cent of the capital of another company, as well as their participation in the management of other business companies or cooperatives as procurators, managers or members of boards, is as follows (as of 31 December 2018) :

Stoyan Mavrodiev – *Chairman of the Board of Directors and Executive Director of the company; he participates in the management of the following companies:*

- Bulgarian Development Bank AD, UIC: 121856059, Chairman of the MB and Chief Executive Director;
- National Guarantee Fund, EAD, UIC: 200321435, a subsidiary of the Bank, as Chairman of the Board of Directors;
- REAL ESTATE VENTURES EOOD, UIC: 131160908 – a sole equity owner;

Rumen Mitrov – *Vice Chairman of the Board of Directors, he participates in the management of:*

- Bulgarian Development Bank AD, UIC: 121856059, as Vice Chairman of the MB and Executive Director;
- Micro Financing Institution Jobs EAD, UIC: 201390740, a subsidiary of the Bank, Chairman of the Board of Directors.

Nikolay Dimitrov – *Member of Board of Directors of the company, he participates in the management of:*

- Bulgarian Development Bank AD, as a member of the MB and Executive Director;
- Micro Financing Institution Jobs EAD, UIC: 201390740, a subsidiary of the Bank, as a member of Board of Directors.

In 2018, there were no material contracts concluded, which lead to action, are amended, or terminated, due to change in the control or as a result of performing a compulsory public procurement procedure, and no such contracts are expected to be concluded.

Transactions with companies under the joint control of the State

Owner of BDB is the Bulgarian state. The consolidated and separate financial statements of the Bank present detailed information regarding the deals of the BDB Group and of BDB with companies under the joint control of the state.

Strategy for development and business goals

The strategic goals of BDB are:

- To facilitate the economic growth by increasing its exposure in support of regions and sectors of the economy with suppressed growth;
- To facilitate the economic growth of the regions through financing, including syndicated, of sizable, strategic and infrastructural, by their nature, projects and investments;
- To support the development of competitive production initiatives and sectors of the economy of proven export potential;
- To facilitate, jointly with the other institutions in the country, the access to financing of innovative and newly established companies (start-ups);
- To facilitate and support the direction of capital flows to the Bulgarian economy.

The BDB Group operates in full transparency and applies the best banking and management practices. A core objective of the Group is to identify and analyse sectors of the economy, in which there are market imperfections and that experience difficulties in accessing and obtaining financing, and to take measures to facilitate their access to funds. The Group supports the export potential and business competitiveness by compensating existing market deficiencies in the financing of certain segments, thereby changing their risk profile and encouraging commercial banks to develop their exposure to them.

These tasks the Bank's Group accomplishes by "completing" the market, while not allowing a "displacing" of commercial banks, and its goal is not to maximize profits.

The Bank adequately assesses the risks assumed and provides credit and warranty lines which, to the maximum extent, allow it to transfer an advantage to customers.

For the effective implementation of the above objectives and tasks, the BDB Group relies on its status as a development bank and the opportunities to attract a long-term and cheap resource, including from international markets.

In future, the BDB Group will continue to offer financing for working capital, capital investments and export finance for small and medium-sized businesses. The Group offers flexible and market-based financial solutions that meet the specificity of the borrower and the project being funded.

Social responsibility and policy of diversity

In 2018, Bulgarian Development Bank continues developing corporate social responsibility by concentrating its efforts most of all towards areas “Vulnerable social groups, “Culture and Art” and “Science and Education”.

In order to perform strictly specific functions as set forth by the BDB Act, the Bank implements a policy of diversity with respect to the administrative, Management and Supervisory Bodies within the powers delegated by the state. The Bank strictly observed the good practices of non-discrimination with respect to age, sex and education.

A cause of the BDB Group is the support of socially vulnerable groups like children and youth deprived of parental care and disadvantaged persons. They believe that charity is a compulsory element not only of corporate social responsibility, but also of the everyday life of each of us, and the employees of the bank concur with this idea.

Vulnerable social groups

Among the initiatives in support of vulnerable social groups the Bank distinguishes the partnership of Bulgarian Development Bank with **Bulgarian Red Cross** in their *The Easter for Everyone National Charity* in support of elderly people, which is held under the auspices of the Ombudsman of the Republic of Bulgaria. The initiative includes provision of financial support to pensioners just before the holidays and is deemed to be very successful as there is a deficit of charity campaigns directed towards this part of the society.

In 2018, the BDB Group also established cooperation with **UNICEF Bulgaria** for the implementation of a pilot project on social care in the districts of Sliven and Shumen. It includes free medical examinations, consultations and practical guidelines for pregnant women and young mothers, with the main aim of preventing problems in early childhood development, neglecting and violence in the family. The Ministry of Health is about to introduce home-based care throughout Bulgaria using the experience of the pilot centres for maternal and child health, and UNICEF will support the process closely through providing technical and expert assistance and training.

The Group successfully partners with **National Fund “St. Nikola” when** performing various initiatives. The Bank supports the fund when organizing creative studios for children and youth, summer rehabilitation camps for children with disabilities deprived of parental care, thematic trips, Christmas and New Year celebrations and other initiatives.

Among the causes supported by BDB is the support for disadvantaged children or children at risk. In 2018, the Bank supported the **SOS Children’s Villages** association in the establishment of a community of foster families and in conducting a summer charity campaign aimed at children and young people deprived of parental care placed in foster families or protected housing. The purpose of the initiative is to organise excursions and summer camps for children at risk, as well as joint activities for children and parents supported by SOS – Centres in Sofia, Pernik, Veliko Tarnovo and Gabrovo. The main task of the campaign is to help children adapt to the new environment and their integration, as well as to conduct targeted individual work with psychologists for deficits and injuries, while at the same time young people are creating positive emotions and experiences.

Traditionally, the **Bulgarian Christmas** is part of the corporate social responsibility of BDB. In 2018, the Bank continued its support to the charity initiative.

Culture and art

The philosophy of BDB is that culture and art unite, cultivate, and bring national pride and sense of belonging. Part of the efforts of the Bank are dedicated to supporting cultural and art-making projects where priority is given to initiatives integrating vulnerable groups through art, motivating young creators, the preservation and promotion of Bulgarian traditions, history, culture.

Among the BDB.s campaigns in this direction in 2018, it could be distinguished the initiative with **a focus on cultural heritage “How Sofia has become a European city”** dedicated to the first city architect of the capital, Antonin Collar. It included an exhibition at the Sofia History Museum (September – October 2018), where there were collected all plans, buildings and public spaces, drawn up by the talented Czech, who 140 years ago committed to the mission to turn the post-Liberation Sofia into a modern European city, as well as the presentation of a documentary on life and work of architect Collar.

The Bank.s Group has continued its efforts to support the preservation of cultural heritage by supporting **a scientific conference** organised by the Sofia History Museum, with the participation of well-established Bulgarian scientists – historians, archaeologists, architects, restaurateurs, whose activity is linked to the preservation of the rich cultural and historical heritage of Sofia and the region.

In this vein, BDB supports also the **International Easter Festival** in the town of Bossilegrad where every year, children from Bulgarian communities both in the country and from Bulgarian diasporas in Serbia, Macedonia, Ukraine, Moldova, and other, take part. Among the goals of the event is the preservation of the customs and traditions in the region.

Bulgarian Development Bank supported the most prestigious classical music ranking in Bulgaria **Musician of the Year 2018**, organised by the Bulgarian National Radio. Prize-winners are renown Bulgarian performers, such as Mincho Minchev, Gena Dimitrova, Rayna Kabaivanska, Krasimira Stoyanova, Vesko Pantelev-Eshkenazi, Yordan Kamdzhlov, Emil Tabakov, Teodosii Spasov. etc. A special prize of BDB – a poster and financial premium for young musicians was established.

In pursuance of its policy to support Bulgarian art, the BDB building is traditionally a host of **temporary exhibitions of paintings and sculptures** of both young and well-established Bulgarian artists.

Education

Bulgarian Development Bank believes that the investments in education and science are investments in the future. Therefore, we have adopted as our own the mission of support for the knowledge seekers, intelligent, talented, ambitious and promising young people in Bulgaria.

Traditionally, BDB Group supports the largest start-up training program in Bulgaria – The Founder Institute-Sofia. The initiative focuses on young entrepreneurs who learn how to develop their ideas into real profitable businesses. In the training process, the most impressive projects reach the successful finals and are formally presented to investors, entrepreneurs and mentors.

In 2018, BDB also helped to implement **the annual study of the Bulgarian digital economy**, which is being prepared by the MOZE.BG Foundation. It aims to map innovative digital start-ups and to explore their history, current and targeted markets, specificities in recruitment, methods of financing, etc. The study covered over 350 companies that meet the criteria for modern digital business and the results provide information on the demography of the Bulgarian digital business and guidelines for the successful development of micro– and small-sized enterprises and start-ups in the sector.

Equal access to education is among the missions that BDB has embedded into its Corporate Social Responsibility Policy. In this respect, in 2018, in cooperation with Vivacom, Bulgarian Development Bank equipped **a computer room at the Center for Family-Type Accommodation** in Gavril Genovo village, where children from

7 to 18 years of age deprived of parental care live. Computer stations Internet, as well as an educational course on initial computer literacy are provided to young people.

The management team in the BDB Group implements focused and consistent actions dedicated to building corporate culture concentrating on the individual and team contribution of the employees towards the realization of the business goals of the Group, as well as the achievement of competitive compensation of the employees as compared to the labour market.

EXECUTIVE DIRECTORS:


RUMEN MITROV


NIKOLAY DIMITROV

**Independent
Auditors'
Report**

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Independent auditors' report To the shareholders of Bulgarian Development Bank AD

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the accompanying consolidated financial statements of Bulgarian Development Bank AD and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at 31 December 2018, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2018, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants (IESBA Code)* together with the ethical requirements of the Independent Financial Audit Act (IFAA) that are relevant to our audit of the consolidated financial statements in Bulgaria, and we have fulfilled our other ethical responsibilities in accordance with the requirements of the IFAA and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

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We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Key audit matter	How our audit addressed the key audit matter
<p>Impairment of loans and advances to customers and related impact from adoption of IFRS 9 "Financial instruments"</p> <p>The Group's disclosures about impairment of loans and advances to customers are included in Note 18 "Loans and advances to customers" and Note 4.1 "Credit risk" with information on the related impact from the adoption of IFRS 9 "Financial instruments" presented and disclosed in Note 2.3 "Changes in accounting policies and disclosures".</p>	
<p>Loans and advances to customers represent a significant part (35%) from the total assets of the Group as at 31 December 2018 with aggregate gross value of BGN 1,211,190 thousand and accumulated loss allowance of BGN 163,156 thousand. The credit risk concentration of the loan and advances portfolio (excluding bank institutions) is disclosed in Note 4.1 "Credit risk". As a result of the adoption of IFRS 9 "Financial instruments", effective 1 January 2018 the Group has implemented a new impairment model based on expected credit loss (ECL) estimation. The reported impact on the opening balance of equity as of 1 January 2018 is BGN 11,435 thousand of additional impairment loss, as disclosed in Note 2.3 "Changes in accounting policies and disclosures".</p> <p>The application of the new impairment model has led to increased complexity and degree of management judgment in the ECL estimations as disclosed in Note 4.1 "Credit risk".</p> <p>The key inputs in the model relate to developing significant increase of credit risk (SICR) criteria for staging of loans and advances to customers (Stage 1: Exposures</p>	<p>In this area, our audit procedures included, amongst others:</p> <ul style="list-style-type: none"> • We gained understanding of the IFRS 9 implementation process of the Group focusing on the ECL impact assessment at the date of initial application, the adopted methodology in the new impairment model and key changes in assumptions and judgements applied. • We evaluated whether the new Group's impairment policy and estimation approaches are in line with the requirements of IFRS 9 and whether the adoption of the Standard is accounted for in accordance with the relevant transitional provisions. • We assessed the Group's governance over the impairment model developed, including the model documentation and the reasonableness and frequency of overlays applied. • We obtained understanding and performed walk-throughs of the Group's processes and controls related to monitoring and evaluating for impairment of loans and advances to customers focusing on any changes as a result of the adoption and post implementation of IFRS 9. We involved

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with no SICR, Stage 2: Exposures with SICR but no objective evidence for impairment and Stage 3: Exposures with objective evidence for impairment), determining the probability of default (PD), the loss given default (LGD) and the exposure at default (EAD), applying also forward looking information (FLI) of macro-economic factors considering multiple scenarios in ECLs estimations.

The higher degree of estimation uncertainty and management judgement is inherent to the estimation of ECLs for the portfolios of loans and advances to customers in Stage 1 and Stage 2 as it is linked to the internal historical data availability for back testing and calibrating the PD and LGD estimates. Further to this, significant management judgement is also required in calculating the ECLs for Stage 3 loans and advances due to inherent estimation uncertainty in determining the timing and amount of the expected cash flows, including the value of the respective collaterals.

Due to the significance of the loans and advances to customers as part of the consolidated financial statements and the credit risk concentration, as well as the high estimation uncertainty, complexity and management judgement involved in ECL calculations under the new impairment model implemented as a result of IFRS 9 adoption, this is considered a key audit matter.

our internal IT specialists to assess and test the IT general controls over these processes.

- We designed and performed tests of the operating effectiveness of the controls over the new impairment model underlying the process for evaluating for impairment of loans and advances to customers and ECL estimation.
- We assessed the new impairment model applied as at both the date of initial application and the reporting date in view of IFRS 9 requirements, the specifics of Group's loan portfolio and the availability of internal historical and forward-looking information. We evaluated the reasonability of SICR criteria and proper staging of loans and advances to customers for a risk-based sample. Further, we assessed for reasonableness the PD and LGD calculations by examining support for the key assumption used and data sources.
- We also analysed whether the forward-looking information have been correlated and considered in the impairment model. In addition, we tested the mathematical accuracy of the ECL calculations.
- We performed analytical procedures on a disaggregated data to evaluate if the relationship in the trends in the recorded impairment expense follow the tendencies of development of the loan portfolios.
- For a risk-based sample of loans and advances to customers from stage 3 and focusing on those with the most significant potential impact on the consolidated financial statements, we specifically assessed the Group's assumptions on the expected future cash flows, including the realizable value of collateral based on our own understanding and available market

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	<p>information. We involved internal experts to assist us in assessing the value of realizable collateral on a sample basis.</p> <ul style="list-style-type: none"> • We performed subsequent events procedures focused on the development of the sampled loans as per the previous paragraph, post balance sheet date to assess the Group's assumptions on the expected future cash flows. • We assessed the relevance and adequacy of the disclosures for the impairment of loans and advances to customers and related impact from adoption of IFRS 9.
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Information Other than the Consolidated Financial Statements and Auditor's Report Thereon

Management is responsible for the other information. The other information, which we have obtained prior the date of our auditor's report, comprises the consolidated management report, including the corporate governance statement prepared by management in accordance with Chapter Seven of the Accountancy Act, but does not include the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon, unless and to the extent explicitly specified in our report.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

Management is responsible for the preparation and presentation of the consolidated financial statements that give a true and fair view in accordance with IFRS, as adopted by the EU, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

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- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves true and fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

We are jointly and severally responsible for the performance of our audit and for the expressed by us audit opinion as per the requirements of the IFAA applicable in Bulgaria. In accepting and executing the joint audit engagement, in connection with which we report hereby, we also have followed the Guidance on Performing a Joint Audit issued on 13 June 2017 by the Institute of Certified Public Accountants in Bulgaria and the Commission for Public Oversight of Statutory Auditors in Bulgaria.

Report on Other Legal and Regulatory Requirements

Additional Matters to be Reported under the Accountancy Act

In addition to our responsibilities and reporting in accordance with ISAs, described above in the *Information Other than the Consolidated Financial Statements and Auditor's Report Thereon* section, in relation to the consolidated management report, including the corporate governance statement of the Group, we have also performed the procedures added to those required under ISAs in accordance with the Guidelines on New and Expanded Auditor's Reports and Auditor's Communication of the professional organisation of certified public accountants and registered auditors in Bulgaria, i.e. the Institute of Certified Public Accountants (ICPA). These procedures refer to testing the existence, form and content of this other information to assist us in forming opinions about whether the other information includes the disclosures and reporting provided for in Chapter Seven of the Accountancy Act and in the Public Offering of Securities Act applicable in Bulgaria.

Translation in English of the official Auditor's report issued in Bulgarian.



Opinion in connection with Art. 37, paragraph 6 of the Accountancy Act

Based on the procedures performed, our opinion is that:

- a) The information included in the consolidated management report referring to the financial year for which the consolidated financial statements have been prepared is consistent with those consolidated financial statements.
- b) The consolidated management report has been prepared in accordance with the requirements of Chapter Seven of the Accountancy Act.
- c) The corporate governance statement of the Group referring to the financial year for which the consolidated financial statements have been prepared presents the information required under Chapter Seven of the Accountancy Act and Art. 100 (m), paragraph 8 of the Public Offering of Securities Act.

Reporting in accordance with Art. 10 of Regulation (EU) No 537/2014 in connection with the requirements of Art. 59 of the Independent Financial Audit Act

In accordance with the requirements of the Independent Financial Audit Act in connection with Art. 10 of Regulation (EU) No 537/2014, we hereby additionally report the information stated below.

- Ernst & Young Audit OOD and Zaharinoва Nexia OOD were appointed as statutory auditors of the consolidated financial statements of Bulgarian Development Bank AD for the year ended 31 December 2018 by the general meeting of shareholders held on 16 August 2018 for a period of one year.
- The audit of the consolidated financial statements of the Group for the year ended 31 December 2018 represents fourth total uninterrupted statutory audit engagement for that group carried out by Ernst & Young Audit OOD and second total uninterrupted statutory audit engagement for that group carried by Zaharinoва Nexia OOD.
- We hereby confirm that the audit opinion expressed by us is consistent with the additional report, provided to the Bank's audit committee, in compliance with the requirements of Art. 60 of the Independent Financial Audit Act.
- We hereby confirm that we have not provided the prohibited non-audit services referred to in Art. 64 of the Independent Financial Audit Act.
- We hereby confirm that in conducting the audit we have remained independent of the Group.

Audit Firm Ernst & Young Audit OOD:

Milka Natcheva-Ivanova
Legal Representative and
Registered Auditor in charge of the audit

Audit Firm Zaharinoва Nexia OOD:

Dimitrina Zaharinoва
Legal Representative and
Registered Auditor in charge of the audit

Sofia, Bulgaria
1 August 2019

Translation in English of the official Auditor's report issued in Bulgarian.

**Consolidated
Annual Financial
Statement**

31 December, 2018

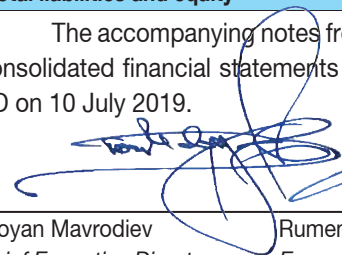
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CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2018

	Note	As at 31.12.2018	As at 31.12.2017
Assets			
Cash in hand and balances in current account with the Central Bank	16	297,622	447,648
Receivables from banks	17	430,003	198,910
Securities at amortised cost		10,216	-
Securities held to maturity	21	-	594
Assets held for sale	25	5,012	10,100
Financial assets at fair value through other comprehensive income	20	653,657	-
Available-for-sale securities		-	291,867
Loans and advances to customers	18	1,048,034	709,111
Current tax liabilities		1,774	1,596
Other assets	26	1,609	1,390
Receivables from the State budget	19	471,999	737,516
Net investment in finance lease	22	932	1,035
Assets acquired from collateral foreclosure	26	27,128	15,875
Investment property	24	7,649	7,702
Property, plant and equipment, intangible assets	23	37,597	32,999
Deferred tax assets	14	261	2,258
Total assets		2,993,493	2,458,601
Liabilities			
Deposits from credit institutions	27	5,759	33,909
Current tax liabilities		22	98
Deposits from customers other than credit institutions	28	1,171,825	659,847
Other liabilities	32	2,780	2,839
Provisions	31	7,828	5,856
Borrowings from international institutions	29	904,782	869,822
Other borrowings	30	110,331	111,406
Total liabilities		2,203,327	1,683,777
Equity			
Share capital	33	601,774	601,774
Retained earnings		27,621	21,995
Revaluation reserve on financial assets measured at fair value through other comprehensive income	34	10,909	11,003
Reserves		149,862	140,052
Total equity		790,166	774,824
Total liabilities and equity		2,993,493	2,458,601


The accompanying notes from 1 to 38 are an integral part of these consolidated financial statements. The consolidated financial statements were approved by the Management Board of Bulgarian Development Bank AD on 10 July 2019.




Stoyan Mavrodiev
Chief Executive Director



Rumen Mitrov
Executive Director



Nikolay Dimitrov
Executive Director



Ivan Lichev
Chief Accountant and
Preparer

Financial statements on which our auditors' report was issued dated 01st of August 2019

"Ernst & Young Audit" OOD



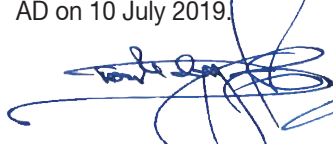
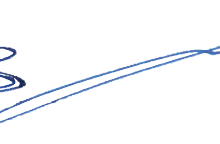
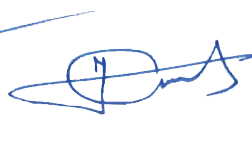

„Zaharina Nexia“ OOD



CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	2018	2017
Interest income	6	66,540	63,278
Interest expense	6	(9,374)	(5,612)
Net interest income		57,166	57,666
Fee and commission income	7	5,679	4,910
Fee and commission expense	7	(69)	(68)
Net fee and commission income		5,610	4,842
Net income on foreign exchange transactions	8	379	409
Net gain/(loss) on financial assets at fair value through other comprehensive income	9	738	188
Other operating income	10	2,461	1,212
Other operating expenses	11	(1,792)	(821)
(Expenses on)/ Income from reversed impairment and provisions	12	(10,046)	(22,095)
Operating income before impairment		54,516	63,496
Cost of personnel	13A	(13,697)	(11,479)
General and administrative expenses	13B	(10,544)	(5,797)
Depreciation / amortisation expenses	23	(1,377)	(1,123)
Profit before income tax		28,898	23,002
Income tax expense	14	(1,811)	(2,322)
Net profit for the year		27,087	20,680
Other comprehensive income			
<i>Items not to be reclassified to profit or loss in subsequent periods:</i>			
Actuarial (losses) / gains on defined benefit plans, net of taxes		33	(63)
<i>Items to be reclassified to profit or loss in subsequent periods</i>			
Net change in fair value of available-for-sale financial assets	15	(343)	4,469
Total other comprehensive income for the year		(310)	4,406
Total comprehensive income for the year		26,767	25,086

The accompanying notes from 1 to 38 are an integral part of these consolidated financial statements. The consolidated financial statements were approved by the Management Board of Bulgarian Development Bank AD on 10 July 2019.

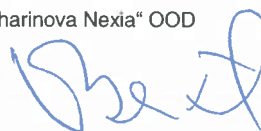
			
Stoyan Mavrodiev Chief Executive Director	Rumen Mitrov Executive Director	Nikolay Dimitrov Executive Director	Ivan Lichev Chief Accountant and Preparer

Financial statements on which our auditors' report was issued dated 01st of August 2019

"Ernst & Young Audit" OOD



„Zaharinoва Nexia“ OOD



CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2018

	Share capital	Statutory reserves	Additional reserves	Revaluation reserve on financial assets at fair value through other comprehensive income	Retained earnings	Total
As of 1 January 2017	601,774	66,159	48,743	6,534	45,842	769,052
Comprehensive income for the period						
Profit	-	-	-	-	20,680	20,680
Other comprehensive income	-	-	(63)	4,469	-	4,406
Total comprehensive income	-	-	(63)	4,469	20,680	25,086
Dividends to equity holders	-	-	-	-	(19,314)	(19,314)
Transfer among the reserves based on shareholders. decision	-	5,830	19,383	-	(25,213)	-
Total transactions with owners	-	5,830	19,383	-	(44,527)	(19,314)
As of 31 December 2017	601,774	71,989	68,063	11,003	21,995	774,824
As of 01 January 2018						
Effect from the initial adoption of IFRS 9	-	-	-	249	(11,684)	(11,435)
As of 01 January 2018 (restated)	601,774	71,989	68,063	11,252	10,311	763,389
Comprehensive income for the period						
Profit	-	-	-	-	27,087	27,087
Other comprehensive income	-	-	33	(343)	-	(310)
Total comprehensive income	-	-	33	(343)	27,087	26,777
Transfer among the reserves based on shareholders. decision	-	1,683	8,094	-	(9,777)	-
Total transactions with owners	-	1,683	8,094	-	(9,777)	-
As of 31 December 2018	601,774	73,672	76,190	10,909	27,621	790,166

The accompanying notes from 1 to 38 are an integral part of these consolidated financial statements. The consolidated financial statements were approved by the Management Board of Bulgarian Development Bank AD on 10 July 2019.

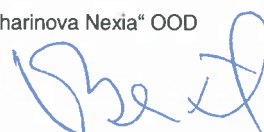
			
Stoyan Mavrodiev Chief Executive Director	Rumen Mitrov Executive Director	Nikolay Dimitrov Executive Director	Ivan Lichev Chief Accountant and Preparer

Financial statements on which our auditors' report was issued dated 01st of August 2019

"Ernst & Young Audit" OOD



„Zaharinoxa Nexia“ OOD



CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	2018	2017
Cash flows from operating activities			
Profit for the year		27,087	20,680
<i>Adjustments for:</i>			
Dividend income	10	(17)	(78)
Expenses / (Income) on / from reversed loan impairment	12	6,021	23,850
Expenses / (Income) on/from guarantee provisions and unutilised credit commitments	12	1,786	(1,917)
Gain on sale of Assets acquired from collateral foreclosure		(437)	(196)
Impairment losses and sale of other assets	26	232	194
Impairment losses and changes in the fair value of financial assets at fair value through other comprehensive income		2,596	-
Effect from the initial adoption of IFRS 9		(11,435)	-
Net gain on revaluation of foreign currency assets and liabilities	8	7	10
Depreciation / amortisation expenses	23	1,378	1,123
Carrying amount of written-off assets	23	1	32
Income tax expense	14	1,811	2,322
		29,030	46,020
<i>Changes in:</i>			
Receivables from banks		13,631	34,427
Loans and receivables		(362,360)	(2,396)
Loans to the State budget		265,517	(313,046)
Available-for-sale securities		-	31,734
Financial assets at fair value through other comprehensive income		(365,508)	-
Net investment in finance lease		70	(317)
Assets held for sale		(3,879)	(5,430)
Other assets		(230)	(969)
Deposits from credit institutions		(28,150)	(9,828)
Deposits from customers other than credit institutions		527,406	82,714
Other liabilities		(946)	1,440
Provisions		2,232	-
Other trade receivables and payables		930	78
Income taxes (paid)		(2,899)	(5,908)
Cash flows used in operating activities		74,844	(141,481)
Cash flows from investing activities			
Cash payments on acquisition of tangible/ intangible assets		(1,178)	(349)
Cash proceeds from sale of tangible/ intangible assets		1	7

CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2018


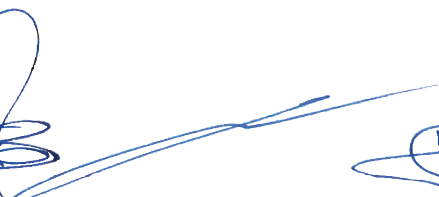


	Note	2018	2017
Proceeds from / (Payments relating to) sale of Assets acquired from collateral foreclosure, and improvements thereof		(2,521)	796
Proceeds from investment property		53	480
Purchase of securities at amortised cost		(10,216)	-
Cash proceeds from maturity of securities held to maturity		593	791
Net cash flows from / (used in) investing activities		(13,268)	1,725

Financing activity			
Dividends paid		-	(19,313)
Cash paid on other borrowings		(3,406)	(2,136)
Cash received from other borrowings		2,331	679
Cash paid on borrowings from international institutions		(121,294)	(67,837)
Net cash flows from financing activity		33,885	468,332

	Note	2018	2017
Net (decrease) / increase in cash and cash equivalents		95,461	328,576
Cash and cash equivalents at the beginning of period	36	522,300	193,724
Cash and cash equivalents at end of period	36	617,761	522,300

Operating interest-related cash flows			
Proceeds from interest		62,271	54,420
Interest paid		(7,909)	(5,290)

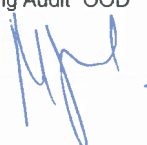
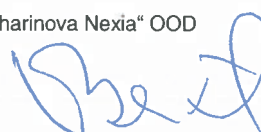
The accompanying notes from 1 to 38 are an integral part of these consolidated financial statements. The consolidated financial statements were approved by the Management Board of Bulgarian Development Bank AD on 10 July 2019.

			
Stoyan Mavrodiev Chief Executive Director	Rumen Mitrov Executive Director	Nikolay Dimitrov Executive Director	Ivan Lichev Chief Accountant and Preparer

Financial statements on which our auditors' report was issued dated 01st of August 2019

"Ernst & Young Audit" OOD

„Zaharinoxa Nexia“ OOD

**Notes to The Consolidated
Financial Statements
for The Year**
Ended 31 December 2018



1. ORGANISATION AND OPERATING POLICIES

The consolidated financial statements of the Group of Bulgarian Development Bank AD (the „Group”) for the year ended 31 December 2018 were approved for issue by decision of the Management Board dated 10 July 2019 (Minutes No. 41 of 10 July 2019).

Bulgarian Development Bank AD is a joint-stock company (AD) registered with the Commercial Register under UIC 121856059, with seat in the city of Sofia, Sofia City Region, Bulgaria, and management address: 1 Dyakon Ignatii Street. The financial year of the Bank ends on 31 December.

Bulgarian Development Bank Group

Bulgarian Development Bank Group (the “Group”) includes the parent-company – Bulgarian Development Bank AD (BDB AD/the Bank) and its subsidiaries – National Guarantee Fund EAD (NGF/ the “Fund”), Micro Financing Institution JOBS EAD (MFI), Capital Investment Fund AD (CIF) and TC Maritsa EOOD.

Bulgarian Development Bank

Bulgarian Development Bank AD (BDB AD/ the “Bank”) was established on 11 March 1999 as a joint-stock company in Bulgaria under the name “Encouragement Bank” AD.

The Bulgarian Development Bank Act was adopted on 23 April 2008 (SG 43/29.04.2008) to regulate the structure and the scope of Bank.s activities, including those for its subsidiaries, envisaged for incorporation. By virtue of that law the functions and all rights and obligations were applied to Encouragement Bank AD. Pursuant to a requirement of the law, a General Meeting of the Shareholders was held (26 June 2008) at which the name of the Bank was changed to Bulgarian Development Bank and its Articles of Incorporation were amended in line with the new legal requirements thereto.

The Bank holds a general banking licence, issued by Bulgarian National Bank (BNB) on 25 February 1999 with latest update of 16 November 2009 (due to the new Credit Institutions Act), and is allowed to conduct all banking transactions permitted by the Bulgarian legislation. The Bank is also a licensed investment intermediary.

From the very beginning, the Bank was established with a special purpose – to support the implementation of the economic policies of the State by financing the business development of small and medium-sized enterprises (SME), including by supporting their investment and export abilities and initiatives. With the adoption of the Bulgarian Development Bank Act in 2008 this objective was further elaborated in the objectives, principles and scope of the Bank.s activities set by the law.

The Bank.s lending activity includes: pre-export and export financing of SME; financing SME operations and projects either through intermediary banks or directly; refinancing banks that grant loans to SME; and financing SME investments abroad.

The main objectives of the Bank are to promote, encourage and develop the general economic, export and technological potential of SMEs by facilitating their access to finance; drawing in and management of medium and long-term local and foreign resources needed for the implementation of economic development in the country; implementation of schemes and instruments to finance public investment projects that are priorities for the country.s economy; fundraising and project management of international financial and other institutions; fundraising and grant funding in order to reduce regional imbalances in the country; financing of projects of local companies that create export, innovation, high employment and / or value added; financing of priority sectors of the economy, in line with the government policy for economic development.

Bulgarian Development Bank AD has a two-tier system of governance, which comprises Supervisory Board (SB) and Management Board (MB). Changes in the structure of the management bodies were not made in 2018. The Supervisory Board and the Audit Committee represent those charged with governance.

As of 31 December 2018, the members of the Supervisory Board of BDB (SB) were: Luchezar Dimitrov Borisov – Chairman of SB, Mitko Emilov Simeonov – Vice Chariman and member of SB, Velina Ilieva Burska – member of SB. The composition of the Management Board of BDB as of 31 December 2018 was as follows: Stoyan Todorov Mavrodiiev – Chairman of MB and Chief Executive Director; Rumen Dimitrov Mitrov – Vice Chairman of MB and Executive Director, Nikolay Dimitrov Dimitrov – member of MB and Executive Director.

The Bank is represented jointly by either two of the three Executive Directors.

As of 31 December 2018, the Bank's employees were 191 (31 December 2017: 171).

Bulgarian Development Bank AD had no branches as at 31 December 2018.

The Bulgarian Development Bank Act (2008) envisages the establishment of two Bank subsidiaries – joint stock companies – the Capital Investment Fund and the National Guarantee Fund.

Capital Investment Fund

The Capital Investment Fund (CIF) was incorporated on 24 August 2018 and entered into the Commercial Register at the Registry Agency on 04 October 2018. The equity owners of Capital Investment Fund AD Bulgarian Development Bank AD holding share of 84.62% and National Guarantee Fund EAD holding share of 15.38%. The management address of the Fund is at 1 Dyakon Ignatii Street. The registered capital as at 31 December 2018 amounted to BGN 65,000 thousand, split into 650,000 registered shares with nominal value of BGN 100 each. The capital paid-in as at 31 December 2018 amounted to BGN 16,250 thousand.

National Guarantee Fund

The National Guarantee Fund (NGF) was established on 12 August 2008 as a sole owner joint-stock company with 100 per cent ownership of BDB. The registered office of the Fund is at 1 Dyakon Ignatii Street, Sofia. As of 31 December 2018, the registered share capital consisted of 800,000 registered nominal shares with par value of BGN 100 each (31 December 2017: 800,000 registered nominal shares with par value of BGN 100 each); the paid-in capital amounted to BGN 80,000,000 as of 31 December 2018 (31 December 2017: BGN 80,000,000).

The scope of NGF's principal activities is defined by the Bulgarian Development Bank Act. It includes:

- a) Issue of guarantees to supplement the collaterals for SME loans;
- b) Provide other guarantee products, suguarantees for participation in tenders good performance guarantees;
- c) Guarantees for advance payments and for payment of loans to exporters;
- d) Other similar services.

The National Guarantee Fund is managed by Board of Directors (BD). In 2018, changes were made in the structure of the management bodies. Members of the board are: Stoyan Mavrodiiev – Chairman, Angel Djalazov – Vice Chairman, Alexander Georgiev – member of the Board of Directors and Procurator.

At 31 December 2018, the NGF employees were 9 (31 December 2017: 12).

Micro Financing Institution JOBS

Micro Financing Institution JOBS EAD (MFI) was incorporated on 23 December 2010 and registered on 14 January 2011 as a sole owner joint stock company, 100 per cent owned by BDB. The registered address of the MFI is at 1 Dyakon Ignatii Street, Sofia. As of 31 December 2018, the registered share capital comprised of 76,430 registered shares with par value of BGN 100 each, and the paid-in capital as of 31 December 2018 amounted to BGN 7,643,000 (as of 31 December 2017, the registered share capital comprised of 76,430 registered shares with par value of BGN 100 each, and the paid-in capital as of 31 December 2017 amounted to BGN 7,643,000.)

The scope of activities is micro-financing including, but not limited to, provision of micro-credits; purchase from third parties and leasing of industrial equipment, automobiles and other vehicles, as well as other assets (financial leasing); sale and purchase of such items; consultancy; trade representation and mediation for local and foreign persons operating in the country, as well as any other activities not prohibited by law.

MFI JOBS EAD is managed by Board of Directors (BD). In 2018, changes were made in the structure of the management bodies.

Members of the Board of Directors:

- **Rumen Dimitrov Mitrov** – *Chairman of the Board of Directors;*
- **Nikolay Dimitrov Dimitrov** – *Vice Chairman of the Board of Directors;*
- **Angel Atanasov Djalazov** – *member of the Board of Directors and Executive Director;*
- **Hristina Atanasova Todorova** – *member of the Board of Directors and Procurator.*

At 31 December 2018 the MFI employees were 11 (31 December 2017: 14).

Bulgarian Development Bank Group had no branches as at 31 December 2018.

Trade Center „Maritsa“

Trade Center „Maritsa“ EOOD became an ownership of Bulgarian Development Bank AD by virtue of decision of the Bank's Management Board in accordance with Minutes No. 29 dated 18 May 2018. The main scope of activity of TC Maritsa includes the operation of concession of the Trade Center, namely a „pedestrian bridge“ in Plovdiv City, in accordance with a contract concluded with Plovdiv Municipality, through setting up trade outlets and collecting rents. The concession contract matures in 2036.

The consolidated financial statements were approved by the Management Board of the parent company (the Bank) on 10 July 2019.

2. BASIS OF PREPARATION OF THE CONSOLIDATED FINANCIAL STATEMENTS, ACCOUNTING ESTIMATES, CHANGES IN ACCOUNTING POLICIES AND PUBLISHED STANDARDS NOT YET EFFECTIVE

These consolidated financial statements have been prepared on a consolidated basis. The Bank prepares separate financial statements in accordance with the Accounting Act. These consolidated financial statements shall be read together with the separate financial statements.

2.1. Basis of preparation

Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards, as adopted by the European Union (IFRS as adopted by the EU). Reporting framework "IFRS as adopted by the EU" is essentially the defined national basis of accounting "IAS, as adopted by the EU", specified in the Bulgarian Accountancy Act and defined in paragraph 8 of its Additional provisions.

- These financial statements have been prepared on a historical cost basis except for the following items-
Financial assets at fair value through profit or loss
- Financial assets at fair value through other comprehensive income
- Financial instruments carried at amortised cost
- Investment property, assets held for sale and assets acquired from collateral foreclosure carried at fair value through profit or loss (Note 3, 5).

Going concern

The Group companies. management assessed their ability to continue their activities as a going concern and is confident about the availability of sufficient resources to continue their normal operations in the foreseeable future. Moreover, management is not aware of any significant uncertainty that could cast doubts as to the ability of the entities to continue operating as a going concern. In view of the above, the separate financial statements of the companies and these consolidated financial statements have been prepared on a going concern basis.

Order of liquidity and maturity structure

In general, the Group presents its consolidated statement of financial position in order of liquidity. An analysis regarding recovery of assets or settlement of liabilities within twelve months after the date of the statement of financial position (current) and more than twelve months after the date of the statement of financial position (non-current) is presented in the notes to the consolidated financial statements.

Presentation currency

The Bulgarian lev is the functional and reporting currency of BDB and its subsidiaries. These consolidated financial statements are presented in thousands of Bulgarian leva (BGN.000).

Methods of consolidation

- These consolidated financial statements have been prepared in accordance with IFRS 10 “Consolidated financial statements”, as all entities over which Bulgarian Development Bank AD has control through ownership of: rights to manage all important activities of the investee;
- exposure or rights to variable return (to obtain benefits or to suffer losses from the activity) from its participation in the entity;
- possibility to exercise control over the investee in order to influence the amount of the return.

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes in one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control over the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Group gains control until the date the Group ceases to control the subsidiary.

The entities consolidated and the consolidation method adopted as at 31 December 2018 are as follows:

Entity	Share	Consolidation method
National Guarantee Fund („NGF“)	100%	full consolidation
Micro Financing Institution JOBS („MFI JOBS“)	100%	full consolidation
TC Maritsa EOOD („TC Maritsa“)	100%	full consolidation
Capital Investment Fund EAD („CIF“)	100%	full consolidation

Upon consolidation all receivables and liabilities, income and expenses, arising from transactions between the Bank and its subsidiaries, are eliminated.

Unrealised losses are eliminated in the same way as the unrealised profit in case there are no indications of impairment. The subsidiaries' financial statements have been prepared for the same reporting period as that of the parent company (the Bank) by applying consistent accounting policies.

2.2. Key estimates and assumptions of high uncertainty

The preparation of the consolidated financial statements in accordance with International Financial Reporting Standards requires management to make judgements, estimates and assumptions that affect the reported amounts of income, expenses, assets and liabilities, and the disclosure of contingent liabilities at the date of the financial statements. These estimates are made on the basis of information available as of the date of the financial statement and therefore, the actual results may differ from these estimates. The items presuming a higher level of subjective assessment or complexity, or where the assumptions and accounting estimates are material for the financial statements, are disclosed in the notes below.

- a) Expected credit losses on assets carried at amortised cost

Monthly, the Group reviews its loan portfolios and other assets carried at amortised cost in order to detect the existence of conditions presuming impairment in the current or future period, and to calculate impairment losses. When assessing whether to include the impairment loss in the statement of comprehensive income, the management of each entity considers whether there are and what are the visible indicators and data, which indicate that there is a measurable reduction in the expected cash flows from the loan portfolio as a whole, or respectively – a decrease associated with a particular loan/component from this portfolio. Such indicators and

data are those that indicate the existence of an adverse change in the payment options by the borrowers from a particular group or by a particular borrower, or the presence of national, economic or other conditions that are associated with a particular risk for a given group/type of loans.

The main indicators for determining the risk groups are the debtor's financial condition and project implementation, funded by the loan, problems with servicing, including interest in arrears and maturing principal, sources of repayment and granted collateral, as a type and opportunity for realisation.

Additionally, for loans, guaranteed by the EIF, the impairment loss is recognised after deduction of the portion borne by the Fund (Note 4.1).

In determining the future cash flows pattern, the Bank's management uses estimates, judgments and assumptions based on its historical loss experience for assets with similar credit risk characteristics, as well as an objective evidence for impairment or expected impairment of the portfolio from unrealised loss in a particular component thereof. Analogous approach is used also for assessments at individual credit exposure, with respect to individually significant loans, taking into account the quality of collateral as well. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly so as to minimize the discrepancies between loss estimates and actual loss experienced (Notes 12, 18 C).

b) Measurement of financial instruments at fair value through other comprehensive income

Equity and debt instruments not quoted on securities exchanges

- The Group classifies as Financial assets at fair value through other comprehensive income its investments held in the form of non-publicly traded companies. shares / entities (less than 20% of their capital), which have been acquired with the aim to establish and develop business relations of interest to the Bank. Management measures these financial assets at fair value using methods that are allowed under IFRS 13, except in cases where it has judged that the cost of acquisition (cost) better reflects their fair value, namely when there is no sufficient and up-to-date information to enable it to measure the fair value; or
- When there is a large scope of eligible methods and/or resultant valuations of the fair value and the cost approximates most closely the fair value within a range of values calculated (Notes 9, 21).

As at 31 December 2018, the Group conducted a thorough comparative analysis of the changes in the movement of market prices on the Bulgarian and foreign securities markets with respect to the shares of public companies and bonds traded publicly held by it.

Equity and debt instruments quoted on exchanges

For investments in securities that are listed for dealing at securities exchanges, the Group has carried out research and analyses and deems that they may be subsequently carried at fair value determined directly on the basis of completed transactions in the market in the last month of the financial year (Level 1). In addition, the applied prices are analysed for trends in the behaviour of market prices of the respective securities at least for the last three months of the year and respectively, to the date of issuing of the separate financial statements of the respective company. (Notes 9, 15, 21).

The Group impairs its debt instruments in compliance with its Policy and Methodology for assessment of expected credit losses and calculation procedure.

c) Provisions for bank guarantees issued

The Group has formed provisions for a portfolio of contingent liabilities for payment in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. The Group reviews its contingent liabilities the

purpose of establishing whether any events have occurred, that would confirm to a large extent the probability that a commitment will be paid to settle an obligation. If such events occur, the Group provides its liability up to the amount of its future costs related to the outflows of economic benefits/payments. These costs/losses are determined on the basis of the present value of the future net cash flows, representing the difference between the payment obligation and the possible inflows of subsequent recourse to the guarantee user or third parties (Notes 12, 35).

d) Actuarial calculations

In assessing the present value of the long-term liabilities to employees upon retirement, actuarial methods and calculations are used based on assumptions for mortality rate, staff turnover rate, future salary levels and a discount factor considered by management as reasonable and relevant to the Bank (Note № 32).

2.3 Changes in accounting policies and disclosures

IFRS 15 Revenue from Contracts with Customers

- IFRS 15 supersedes IAS 11 Construction Contracts, IAS 18 Revenue and related Interpretations and it applies, with limited exceptions, to all revenue arising from contracts with customers and not covered by the scope of Lease contracts (IAS 17/IFRS 16 Leases);
- Insurance contracts (IFRS 4 Insurance contracts);
- Financial instruments and other contractual rights or obligations (IFRS 9 Financial Instruments, IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Ventures, IAS 27 Separate Financial Statements, and IAS 28 Investments in Associates and Joint Ventures);
- Non-monetary transactions among entities engaged in the same business to facilitate the sales to customers or potential customers.

The Group has applied IFRS 15 effective for annual periods beginning on or after 1 January 2018.

IFRS 15 establishes a five-step model to account for revenue arising from contracts with customers, regardless of the type of transaction or industry, requiring the Group (1) to identify the contracts with customers, (2) to identify the performance obligations in the contracts, (3) to determine the transaction price, (4) to allocate the transaction price to the performance obligations, and (5) to recognise revenue when each performance obligation is satisfied.

The Group has identified the following three performance obligations under IFRS 15:

- Transaction-related services – revenue is recognised at a point in time as the customer simultaneously receives and consumes the benefits due to the short time period of performance of the service. The fees for these services are based on the published tariff and represent a fixed amount per transaction corresponding to the customer's benefit transferred. Considering the above circumstances, the Group applies the practical expedient under IFRS 15, paragraph B16, namely, to recognise revenue in an amount it has the right to withhold in accordance with the Tariff. Under IAS 18, the Group used to recognise revenue by applying the accrual principle and thus, it recognised revenue in the same way.
- Issuance of guarantees and letters of credit – revenue is recognized over time because the customer simultaneously receives and consumes the benefits. The transfer of the benefits to the customer is consistent over time and thus, the Group uses a straight-line method for measuring the progress of the contract, which in turn results in a straight-line amortisation of the fees over the contracted period. The fees for these services are fixed, calculated depending on the amount of the guarantee or the letter of credit.

Under IAS 18, The Group used to recognize revenue from the fixed fee over the term of the contract on a straight-line basis, which in substance is identical with the accounting policy under IFRS 15.

- Account maintenance – revenue is recognised at a point in time because the customer simultaneously receives and consumes the benefits. The fees for these services are based on the Tariff and represent a fixed monthly amount corresponding to the customers. benefit transferred. Considering the above circumstances, the Group applies the practical expedient under IFRS 15, paragraph B16, namely, to recognise revenue in an amount it has the right to withheld in accordance with the Tariff. Under IAS 18, the Group used to recognise revenue by applying the accrual principle and thus, it recognised revenue in the same way.

Brokerage operations for which the Group receives agent.s commissions– revenue is recognised at a point in time upon the provision of the brokerage service as the Group operates as a broker. Considering the above circumstances, the Group recognizes revenue that is equal to the amount of the commission fee for the performance of the brokerage service. The commission fee is the net amount to be withheld by the Group company after paying the portion due to the third party to which / whom the Group has mediated to perform the services of that third party.

Fee and commission income of Bulgarian Development Bank Group for 2018 and 2017 are as follows:

Fee and commission income	2018	2017
Transaction-related services*	1,630	-
Issuance of guarantees and letters of credit	3,945	-
Account maintenance	69	-
Total fee and commission income from contract with customers	5,644	-
Other charges	35	-
Total fees and commissions 2018	5,679	-
Guarantees and letters of credit	-	3,323
Account maintenance, transfers and customers. treasury operations	-	560
Servicing of debt issues	-	252
Special-purpose funds of the Ministry of Agriculture and Foods and Executive Agency Fisheries and Aquacultures (Note 30)	-	679
Special-purpose funds of the Ministry of Finance (Note 30)	-	64
Others	-	32
	-	4,910
Fee and commission expenses		
Agent.s commissions	(34)	(30)
Transfers and cash transactions with other banks	(4)	(3)
Servicing of accounts with other banks	(31)	(35)
Total fee and commission expenses	(69)	(68)
Net fee and commission income	5,610	4,842

*The transaction-related services include operation on a trust basis of funds of special-purpose funds of the Ministry of Agriculture and Foods and Executive Agency Fisheries and Aquacultures: BGN 1,039 thousand, and of special-purpose funds of the Ministry of Finance: BGN 62 thousand. Further details of the programmes are given in Note 30. They are presented on separate lines for 2017.

Fees for servicing debt issues fees are charged for performing the function of a trustee bank on a bond issue of a public interest entity. The fee is charged and paid periodically, in accordance with a contract.

The Group – except for certain operations provided to its employees – earns no income from retail banking services: the amount of deposits accepted as at 31 December 2018 is immaterial (BGN 967 thousand), as also the number of accounts opened.

The Group has not analysed in detail the potential effect of such services on revenue due to its limited exposure to retail customers and the absence of branch network.

IFRS 9 Financial instruments: classification and measurement

The standard is effective for annual periods beginning on or after 1 January 2018. The Group has decided not to apply it earlier. The Group has elected not to restate items on the statement of financial position and the income statement for previous periods in accordance with the new standard any differences arising until 31 December 2017 are included in Retained earnings/(losses).

In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments that replaces IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for financial instruments project: classification and measurement, impairment and hedge accounting. Except for hedge accounting, retrospective application of the standard is required but providing comparative information is not compulsory. For hedge accounting, the requirements are generally applied prospectively, with some limited exceptions.

Initial adoption of IFRS 9

- The group applied for the first time IFRS 9 in 2018. In the months preceding 1 January 2018, the Group.s management approved a standard implementation program, including: Review of the classification and measurement of financial assets in view of their compliance with the classification and measurement criteria of IFRS 9, and introduction of new accounts in the Group.s accounting system;
- Development of a new financial asset impairment methodology;
- Introduction of changes in information systems and processes in cases when there is a contractual requirement governing the instrument.

Asset recognition

The Group recognizes a financial asset or financial liability in its statement of financial position when, and only when, the Group classifies financial assets as subsequently measured at amortised cost, at fair value in other comprehensive income or at fair value through profit or loss, as the case may be, on the grounds of:

- a) a business model of the Bank for financial assets management (or a sub-portfolio of financial assets), and
- b) the features of the contractual cash flow of the financial asset.

Regardless of its election with regard to the reporting approach, the Group has the option, at initial recognition, to irrevocably designate a financial asset as measured at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases, as per the paragraphs below:

- a) If the Group has liabilities under insurance contracts whose measurement incorporates current information and financial assets that it considers to be related and that would otherwise be measured at either fair value through other comprehensive income or amortised cost;
- b) If the Group has financial assets, financial liabilities or both that share a risk, and that gives rise to opposite changes in fair value that tend to offset each other;
- c) If the Group has financial assets, financial liabilities or both that share a risk, that gives rise to opposite changes in fair value that tend to offset each other and none of the financial assets or financial liabilities qualifies for designation as a hedging instrument because they are not measured at fair value through profit or loss.

A financial asset is measured at amortised cost, if both of the following two criteria are met simultaneously:

- a) The financial asset is held within a business model with the objective to collect their contractual cash flows (Hold to Collect business model); and
- b) The contractual terms of the financial asset lead to generation of cash flows that are solely payments of principal and interest on the outstanding interest, on specific dates (SPPI).

A financial asset is measured at fair value in other comprehensive income, if both of the following two criteria are met simultaneously:

- a) The financial asset is held within a business model with the objective to collect the contractual cash flows and sell the financial asset, and
- b) The contractual terms of the financial asset lead to generation of cash flows that are solely payments of principal and interest on the outstanding principal, on specific dates.

A financial asset is measured at fair value through profit or loss, unless it is measured at amortised cost or at fair value in other comprehensive income in accordance with the above criteria.

Upon initial recognition, the Group may make an irrevocable choice to include in fair value in other comprehensive income subsequent changes to an investment in an equity instrument that is not held for trading or is not a contingent remuneration recognised by a transferee in a business combination to which IFRS 3 applies.

The effect of initial adoption of IFRS 9 as at 1 January 2018 compared to IAS 39 as of 31 December 2017 was, as follows:

IAS 39		As of 01.01.2018		IFRS 9	
Financial assets	Category	Amount	Effect of adoption of IFRS 9	Amount	Category
Cash in hand and balances in accounts with the Central Bank	Loans and receivables	447,648	-	447,648	Amortised cost
Loans and advances to central banks and government	Loans and receivables	737,516	(1,432)	736,084	Amortised cost
Loans and advances to central banks and financial institutions	Loans and receivables	200,469	(3,355)	197,114	Amortised cost
Loans and advances to customers	Loans and receivables	715,700	(4,989)	710,711	Amortised cost
Financial assets available for sale	Available for sale/Held for trading	292,461	(460)	292,001	Fair value through OCI

	IAS 39	As of 01.01.2018	IFRS 9
Total financial assets	2,393,794	(10,236)	2,383,558
Financial liabilities			
Borrowings	1,719,960	-	1,719,960
Expected losses on credit guarantees	4,961	449	5,410
Provisions	930	-	930
Total financial liabilities	1,725,851	449	1,726,300
Off-balance sheet exposures	844,965	(750)	844,215

Reclassification of financial assets

When and only when the Group changes its business model for financial asset management, it reclassifies all financial assets affected, in line with the asset classification requirements. If the Group applies such reclassification to financial assets, it shall apply it in the future from the reclassification date. The Group does not recalculate previously recognised profits, losses (including gains or impairment losses) or interest.

Assessment and reporting

Upon initial recognition, in the case of a financial asset or financial liability not stated at fair value through profit or loss, the Group measures a financial asset or a financial liability at fair value, taking into account as a probable increase and/or decrease of the transaction costs which are directly related to the acquisition or creation of the financial asset or financial liability.

Determination of a business model

The Group defines the **“business model with the objective to collect their contractual cash flows (Hold to Collect business model)”** as a business model where the Group.s financial assets are managed with the objective to generate cash flows through collection of contractual cash flows over the instrument.s lifetime. The Group may use this business model in the event of converting the sale of assets with increased credit risk or in order to reduce the concentration risk. These financial assets are carried at amortised cost.

The Group defines the **“business model with the objective to collect the contractual cash flows and sell the financial asset”** as a business model where the Group.s key management staff have decided that the collection of contractual cash flows and the sale of financial assets are an integral part of the achievement of the business model.s objective and includes much more frequent and of higher value sales of financial assets than a business model with the main purpose of holding financial assets to collect contractual cash flows. These assets are reported as financial assets at fair value through other comprehensive income.

The Group defines **“Other business models”** as a business model that does not include the holding of financial assets for the purpose of collecting contractual cash flows or for the simultaneous collecting of contractual cash flows and selling financial assets. Typically, this process involves actively buying and selling financial assets.

These assets are reported as financial assets at fair value through profit or loss or through other comprehensive income, as the case may be.

In this respect, as of 1 January 2018 and 31 December 2018, the Group has defined the following classification of the main financial assets:

- Financial assets carried at fair value through profit and loss – they will be recognised as financial assets at fair value through profit or loss;
- Financial assets available for sale – they will be recognised as financial assets at fair value in other comprehensive income;
- Loans and advances to clients – they will be recognised as financial assets at amortised cost;
- Financial assets held to maturity – they will be recognised as financial assets at amortised cost;
- Other receivables – they will be recognised as financial assets at amortised cost;

The Group derecognises financial asset when, and only when:

- the contractual cash flows from the financial asset have expired, or
- the financial asset has been transferred and this transfer meets the derecognition criteria.

Impairment of financial assets (incl. lease)

IFRS 9 fundamentally changes financial asset impairment reporting, by replacing the existing incurred credit loss model with a forward-looking expected credit loss (ECL) model. IFRS 9 requires that impairment is recognized not only for non-performing loans, but instead for all loans, receivables from banks, receivables under leased contracts and debt instruments not measured at fair value in other comprehensive income, as well as the accrual of provisions for credit engagements and financial guarantees. The amount of the impairment depends on the probability of default of the debtor over the next 12 months after initial recognition, unless there has been a significant increase in credit risk, which requires the estimation of expected credit losses over the lifetime of the financial asset.

The estimate of ECLs is based on all available, reasonable and justified information at the reporting date for past events, the current situation and the use of relevant macroeconomic indicators and reliable forecasts of future economic conditions.

The key macroeconomic indicators, used by the Group, are gross domestic product, unemployment, inflation, changes in oil prices, and changes in the USD exchange rate and 3M EURIBOR. The expected credit losses for loans classified in Phase 3 are measured on the basis of three macroeconomic scenarios – realistic, negative and optimistic, which are used in the calculation of the impairment by applying different weights. The results obtained can be further adjusted and expected credit losses increased or reduced to reflect future risks that cannot be modelled (mainly, legislative or regulatory).

The Group has drawn up a methodology that introduces criteria for classifying financial assets in three categories (the so-called “phases”), transfer criteria between them and setting an impairment amount depending on the phase in which the underlying asset is classified.

The phases and their characteristics are described below:

- Phase 1 – includes standard (performing) loans without a significant increase in credit risk after initial recognition. The impairment of those assets is based on the probability of default of the debtor over the next 12 months or for a shorter period if the life of the instrument is shorter than one year.
- Phase 2 – includes assets with a significant increase in credit risk after initial recognition. Such an increase is presumed if the loan is past due for more than 30 days; the debtor is placed on watch; the debtor's credit rating has deteriorated at the reporting date compared to its rating on the date of recognition of the instrument, or the Group expects the credit to be restructured. In this case, the expected credit losses are calculated for the entire lifetime of the asset;

- Phase 3 – includes assets, for which objective evidence exists that they are impaired, such as non-performing loans. The Group has set specific criteria that determine when a debtor is in default. The expected credit losses for these instruments are also calculated for the entire lifetime of the instrument.

The absolute threshold for the transfer of credits among the levels is linked to the internal credit rating determined by the Group of the borrower concerned. The Group has set a credit rating of 7 as a transition limit to move to Phase 2.

For financial assets comprising receivables under lease contracts, the expected credit loss is determined by cash flows compatible with cash flows used to measure the receivable under lease contract in accordance with IAS 17.

The expected credit losses under lease contracts are discounted using the same discount rate which has been used to measure the lease receivables in accordance with IAS 17.

IFRS 16, which is effective for annual periods beginning on or after 1 January 2019 and replaces IAS 17, does not change significantly the reporting of lease contracts by lessors and therefore, the Group does not expect any considerable effect or significant changes in 2019 onwards.

Hedge accounting

IFRS introduces a significant amendment to hedge accounting, requiring more extensive disclosures regarding the risk management activity. The Group's business model does not provide taking of significant market or foreign currency positions. Insofar as the Group is exposed to currency or interest rate risk, it takes appropriate measures to minimize that risk: matching the amount of active and passive exposures in the relevant currency, providing coverage of interest-bearing fixed-rate assets with similar interest-bearing fixed-rate liabilities.

The Group fully assumes the market risk arising out of its securities regardless of whether they have been held to collect cash flows or to sell.

The Group has no foreign subsidiaries to be consolidated.

The Group does not report active financial instruments designated as hedging relationships and therefore, the requirements of IFRS 9 applicable to hedges have no effect on the Group's financial statements.

IFRS 2 Share-based Payment (Amendments): Classification and Measurement of Share based Payment Transactions

The amendments are effective for annual periods beginning on or after 1 January 2018 with earlier application permitted. The amendments provide requirements on the accounting for the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments, for share-based payment transactions with a net settlement feature for withholding tax obligations and for modifications to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled. The amendments were endorsed by the EU in February 2018. The amendments are not relevant for the Group.

IFRS 4 Insurance Contracts (Amendments): Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts

The amendments are effective for annual periods beginning on or after 1 January 2018. The objective of these amendments is to address issues arising from the different effective dates of IFRS 9 Financial Instruments and the upcoming new insurance contracts standard IFRS 17 Insurance Contract. Entities issuing insurance contracts will still be able to adopt IFRS 9 on 1 January 2018. The amendments introduce two alternative options for entities issuing contracts within the scope of IFRS 4, notably a temporary exemption and an overlay approach.

The temporary exemption enables eligible entities to defer the implementation date of IFRS 9. The overlay approach allows an entity applying IFRS 9 from 2018 onwards to remove from profit or loss the effects of some of the accounting mismatches that may occur from applying IFRS 9 before IFRS 17 is applied. The standard had no significant impact on the financial performance and operating results of the Group in 2018. The Group does not expect that the standard will have a significant impact in the future as well.

IFRIC 22 Foreign Currency Transactions and Advance Consideration

The interpretation is effective for annual periods beginning on or after 1 January 2018 with earlier application permitted. This interpretation addresses how to determine the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) on the derecognition of a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration in a foreign currency. The interpretation was endorsed by the EU in April 2018. The interpretation had no significant impact on the financial performance and operating results of the Group in 2018. The Group does not expect that the interpretation will have a significant impact in the future as well.

IAS 40 Investment Property (Amendments): Transfers of Investment Property

The amendments are effective for annual periods beginning on or after 1 January 2018 with earlier application permitted. The amendments clarify transfers of property to, or from, investment property when there is a change in the use of such property which is supported by evidence. The amendments were endorsed by the EU in March 2018. The amendments had no significant impact on the financial performance and operating results of the Group in 2018 and it is not expected that they will have a significant impact on its future financial statements.

Annual Improvements to IFRSs 2014-2016 Cycle

- In the 2014-2016 annual improvements cycle, the IASB issued amendments to standards, which are effective for annual periods beginning on or after 1 January 2018. Summary of amendments and related standards are provided in IFRS 1 First-time Adoption of International Financial Reporting Standards – deletion of short-term exemptions for first-time adopters;
- IFRS 12 Disclosure of Interests in Other Entities – clarification of the scope of the Standard (IASB effective date: 1 January 2017, however the EU endorsement is after that date)
- IAS 28 Investments in Associates and Joint Ventures – measuring an associate or joint venture at fair value.

The annual improvements to IFRSs 2014 – 2016 Cycle were endorsed by the EU in February 2018. These amendments had no significant impact on the financial performance and operating results of the Group in 2018.

2.4 Standards issued but not yet effective and not early adopted

Standards issued but not yet effective or not early adopted up to the date of issuance of the Group's financial statements are listed below. This listing is of standards and interpretations issued, which the Group reasonably expects to have an impact on disclosures, financial position or performance when applied at a future date. The Group intends to adopt those standards when they become effective.

IFRS 16 Leases

- The standard is effective for annual periods beginning on or after 1 January 2019. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor'). The new standard requires lessees to recognize most leases on their balance sheet and to have a single accounting model for all leases, with certain exemptions. Lessor accounting is substantially unchanged. The Group has analysed the potential impact of the adoption of this standard on its financial position or performance. The Group as a lessee – considering the minimum leased assets being used – with carrying amount of BGN 698 thousand as at 31 December 2018 – the Group deems the effect of the adoption of IFRS 16 immaterial.
- The Group as a lessor – considering that IFRS 16 preserves to a large extent the treatment stipulated in IAS 17, the Group deems that the effect of its adoption would not be significant.

IFRS 17: Insurance Contracts

The standard is effective for annual periods beginning on or after 1 January 2021 with earlier application permitted if both IFRS 15 Revenue from Contracts with Customers and IFRS 9 Financial Instruments have also been applied. IFRS 17 Insurance Contracts establishes principles for the recognition, measurement, presentation and disclosure of insurance contracts issued. It also requires similar principles to be applied to reinsurance contracts held and investment contracts with discretionary participation features issued. The objective is to ensure that entities provide relevant information in a way that faithfully represents those contracts. This information gives a basis for users of financial statements to assess the effect that contracts within the scope of IFRS 17 have on the financial position, financial performance and cash flows of the Group. The standard has not been yet adopted by the EU.

IFRIC 23 Uncertainty over Income Tax Treatments

The Interpretation is effective for annual periods beginning on or after 1 January 2019 with earlier application permitted. The Interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS 12. The Interpretation provides guidance on considering uncertain tax treatments separately or together, examination by tax authorities, the appropriate method to reflect uncertainty and accounting for changes in facts and circumstances. This interpretation was endorsed by the EU in October 2018. The Group does not expect a significant impact of this interpretation on its financial statement and financial performance in future periods.

IAS 28 Investments in associates (Amendments): Long-term Interests in Associates and Joint Ventures

The amendments are effective for annual periods beginning on or after 1 January 2019 with earlier application permitted. The Amendments clarify that an entity applies IFRS 9 Financial Instruments to long-term interests in

an associate or joint venture that, in substance, form part of the net investment in the associate or joint venture but to which the equity method is not applied. An entity applies IFRS 9 to such long-term interests before it applies IAS 28. In applying IFRS 9, the entity does not take account of any adjustments to the carrying amount of long-term interests that arise from applying IAS 28. These amendments have not yet been adopted by the EU.

IAS 19 Employee Benefits (Amendments): Plan Amendment, Curtailment or Settlement

The amendments are effective for annual periods beginning on or after 1 January 2019 with earlier application permitted. The amendments require entities to use updated actuarial assumptions to determine current service cost and net interest for the remainder of the annual reporting period after a plan amendment, curtailment or settlement has occurred. The amendments also clarify how the accounting for a plan amendment, curtailment or settlement affects applying the asset ceiling requirements. These amendments have not yet been adopted by the EU. The Group is in the process of assessing the impact of these amendments on its financial position or performance.

IFRS 3 Business combinations (Amendments): Definition of a business

The amendments are effective for annual periods beginning on or after 1 January 2020 with earlier application permitted. The amendments clarify the minimum requirements for a business and narrow the definition of a business. The amendments also remove the assessment of whether market participants are capable of replacing any missing elements, add guidance to help entities assess whether an acquired process is substantive and introduce an optional fair value concentration test. These amendments have not yet been endorsed by the EU.

Amendments to IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors: Definition of 'material'

The amendments are effective for annual periods beginning on or after 1 January 2020 with earlier application permitted. The amendments clarify the definition of material and how it should be applied by including in the definition guidance that until now has featured elsewhere in IFRS Standards. The amendments also specify that materiality will depend on the nature or magnitude of information. These amendments have not yet been adopted by the EU.

The Conceptual Framework for Financial Reporting

The IASB issued the revised Conceptual Framework for Financial Reporting on 29 March 2018, which is effective for annual periods beginning on or after 1 January 2020. The Conceptual Framework sets out a comprehensive set of concepts for financial reporting, standard setting, guidance for preparers in developing consistent accounting policies and assistance to others in their efforts to understand and interpret the standards. The main amendments introduced in the revised Conceptual framework for financial reporting are related to measurement, including factors, which should be considered when choosing measurement basis, and to presentation and disclosure, including income and expenses which should be classified in other comprehensive income. The Conceptual framework also provides updated definitions for asset and liability and criteria for their recognition in the financial statements. The Conceptual framework for financial reporting has not yet been adopted by the EU.

Annual Improvements to IFRSs 2015-2017 Cycle

In the 2015-2017 annual improvements cycle, the IASB issued amendments to standards which are effective for annual periods beginning on or after 1 January 2019. Summary of amendments and related standards are provided below:

- IFRS 3 Business Combinations and IFRS 11 Joint Arrangements – clarifying previously held interest in a joint operation;
- IAS 12 Income taxes – clarifying income tax consequences of payments on financial instruments classified as equity;
- IAS 23 Borrowing costs – clarifying borrowing costs eligible for capitalization.

The annual improvements to IFRSs 2015 – 2017 Cycle were endorsed by the EU in March 2019. The Group is in the process of assessing the impact of the amendments on its future financial statements.

Amendments to IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates and Joint Ventures: Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

The amendments address an acknowledged inconsistency between the requirements in IFRS 10 and those in IAS 28, in dealing with the sale or contribution of assets between an investor and its associate or joint venture. A full gain or loss is recognized when a transaction involves a business or a partial gain or loss is recognized when a transaction involves assets that do not constitute a business. The IASB postponed the effective date of this amendment indefinitely pending the outcome of its research project on the equity method of accounting. The amendments have not yet been adopted by the EU.

3. SIGNIFICANT ACCOUNTING POLICIES

3.1 Financial instruments

The Group initially recognises loans, receivables (incl. under leases) and deposits on the date they were incurred. All other financial instruments (including assets and liabilities designated at fair value through profit or loss) are recognised initially on the trade date, which is the date that the Bank becomes a party to the contractual provisions of the instrument.

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or the Bank transfers the rights to receive the contractual cash flows in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in such transferred financial asset that qualify for derecognition, which is created or retained by the Bank, is recognised as a separate asset or liability.

Financial assets and liabilities are offset and the net amount presented in the separate statement of financial position when, and only when, the Bank has a legal right to set off the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

The Bank has the following non-derivative financial assets:

- financial assets at fair value through profit or loss;
- financial assets at fair value through other comprehensive income;
- financial assets at amortised cost;

Financial assets at fair value through profit or loss in accordance with IFRS 9

A financial asset is carried at fair value through profit or loss if it is held for trading or if it is designated as such upon initial recognition. Financial assets are designated at fair value through profit or loss when the Bank manages them and makes decisions for purchases and sales on a fair value basis, in accordance with a documented risk or investment management strategy of the Bank. Attributable transaction costs are recognised in profit or loss as incurred.

Financial assets at fair value through profit or loss are measured at fair value and any related changes, including dividend income, are recognised in profit or loss.

Upon initial acquisition, the Bank's management determines whether a financial assets will be held for trading. Usually, management designates derivatives as such instruments.

A derivative is a financial instrument:

- Whose value changes in response to changes in interest rates, security prices, commodity prices, foreign exchange rates, price indices or interest rates, credit ratings or credit indices, or other variables;
- That requires no initial net investment, or one that is smaller than would be required for a contract with similar response to changes in market conditions;
- That is settled at a future date.

When upon entering a specific derivative transaction, the Bank defines a position to be hedged and all the requirements of IFRS 9 have been met, the corresponding derivative is recognised as such hedging and it shall be specified whether it hedges:

- deviations in the fair value of a specific asset (fair value hedge),
- differences in the estimated future cash flows (cash flow hedge), or
- the effect of investments in foreign subsidiaries (net investment hedge).

Derivatives that do not meet the criteria for hedge accounting are measured at fair value through profit and loss. Initially, derivative financial instruments are measured at cost (including transaction costs) and subsequently, they are measured at fair value. Derivatives are accounted for as assets when their fair value is positive and as liabilities when it is negative.

Financial assets measured at amortised cost in accordance with IFRS 9

Financial assets measured at amortised cost are financial assets with fixed or determinable payments that are not quoted in an active market and that are 'solely payments of principal and interest (SPPI)'. The Bank holds such financial assets within a business model with the objective to hold financial assets in order to collect contractual cash flows within the life of the asset. Such assets are initially measured at fair value plus incremental direct transaction costs. Subsequently, loans and receivables are measured at their amortised cost using the effective interest rate, less any impairment losses. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument, or, where appropriate, a shorter period, to the present carrying amount of the financial asset or liability.

When calculating the effective interest rate, the Bank estimates the cash flows by considering all contractual terms of the financial instrument, but not considering any future credit losses.

The calculation includes all charges and other fees paid to or received by the contractors that are an integral part of the effective interest rate.

The Group assesses whether evidence of impairment of loans and receivables exists for each specific asset, except for receivables from employees (Note 3: Impairment of financial assets) and receivables under EEMFBNP. After a thorough review of the quality and impairment testing of standard exposures, the Bank established that as at 31 December 2018, as also in 2017, the expected credit loss on receivables from employees was 0%, and that which had arisen from receivables having occurred in relation to Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP) amounted to BGN 804 thousand (as at 01 January 2018, after considering the effect of the adoption of IFRS 9: BGN 1,432 thousand, as at 31 December 2017: Nil).

Financial assets measured at amortised cost cash and cash equivalents, receivables from banks, loans and advances to customers, receivables from the State budget, and trade and other receivables.

Financial assets at fair value through other comprehensive income in accordance with IFRS 9

Financial assets measured at fair value through other comprehensive income are assets acquired under a business model with the objective of both holding to collect contractual cash flows and selling; and that are not classified in any one of the previous categories. Subsequent to initial recognition, they are measured at fair value and any fair value changes, other than impairment losses (Note 3: Impairment of financial assets), and foreign exchange gains or losses on debt instruments, are recognised in other comprehensive income and presented in the fair value reserve as part of equity. When an investment is derecognised, the accumulated gains or losses in other comprehensive income are reclassified to profit or loss.

Financial assets measured at fair value through other comprehensive income include equity and debt securities, and certain cases of loans and advances.

Finance lease receivables in accordance with IAS 17

Lease activity in the Group is associated with leasing out of industrial equipment, vehicles, agricultural machinery etc. on financial lease terms. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incident to ownership.

All other leases, which do not transfer risk and rewards incident to ownership of the asset, are classified as operating lease.

Minimum lease payments

Minimum lease payments are the payments over the lease term that the lessee is or can be required to make. From the Group's perspective, the minimum lease payments also include the residual value of the asset, which is guaranteed by a third party unrelated to the Group, under the condition that this third party is financially capable of discharging the obligation under the guarantee or the sale back agreement. The minimum lease payments comprise also the price of exercising an option of the lessee to purchase the asset, when at the inception of the lease it is virtually certain that this option will be exercised.

Minimum lease payments exclude any contingent rent, cost for services and taxes paid by the Group and subsequently re-invoiced to the lessee.

Commencement of the lease contract and commencement of the lease term

There is a distinction between the commencement of the lease contract and the commencement of the lease term:

- The commencement of the lease contract is the earlier of the two dates: the date of the lease contract or the date of the commitment by the parties to the main terms and conditions of the lease contract.
- The commencement of the lease term is the date from which the lessee may exercise the right to use the leased asset. This is the date at which the Group initially recognises the lease receivable.

Initial measurement and subsequent recognition

Initially, the Group recognises a finance lease receivable, which is equal to its net investment in the lease comprising the present value of the minimum lease payments and any unguaranteed residual value for the Group. The present value is calculated by discounting the minimum lease payments at the interest rate implicit in the lease. Any initial direct costs are added to the finance lease receivable. During the lease term, the Group accrues financial income (interest income on finance lease) over the net investment. The lease payments received are treated as a reduction of net investment (repayment of the principal) and recognition of finance income in such a way that ensures a constant rate of return on the net investment.

Subsequently, the net investment in finance leases is presented net, less any individual and portfolio allowance for uncollectability.

The impairment loss is measured as the difference between the carrying amount and the present value of estimated future cash flows discounted at the original effective interest rate. The impairment loss is recognised in profit or loss and reported in an allowance account reducing the amount of finance lease receivables. When an event, which has occurred after an impairment has been recognised, reduces the impairment loss, this reduction is reversed through profit or loss.

Reclassification of financial assets

According to the treatment of IFRS 9, financial assets are reclassified only if the business model in which the assets are acquired and/or managed is changed. Upon such a change, the Group reclassifies all affected assets from one category to the other.

Assets under trust management

The Group provides trust management services that includes holding of or investing in assets on behalf of customers. Assets held under trust management, unless certain recognition criteria have been met, are not included in the Group's financial statements since they are not assets of the Group.

Bulgarian Development Bank, a group entity, performs services in its capacity as an investment intermediary in accordance with the provisions of the Public Offering of Securities Act (POSA). Being an investment intermediary, the Bank is obliged to comply with certain requirements in order to protect its customers' interests in accordance with the Markets in Financial Instruments Act (MFIA) and Ordinance 38, issued by the Financial Supervision Commission (FSC). Moreover, the Bank should also observe the requirements of Directive 2014/65/EU on the Markets in Financial Instruments (MiFID II) and Regulation 600/2014 of the EU on the Markets in Financial Instruments (MiFIR). The Bank has developed and implements organization relating to the conclusion and performance of contracts with customers, the requirement of information from customers, keeping records and storage of clients' assets, in compliance with the provisions of the above-mentioned National and European legal acts. The Bank has implemented a system of in-house internal control rules and procedures aiming at ensuring its full compliance with the bodies of legislation mentioned above.

Financial liabilities

Financial liabilities, which are not derivative instruments or which have not been designated on acquisition as liabilities to be measured at fair value through profit or loss, are measured at amortised cost. Initially, they are stated at "cost", i.e. the fair value of cash flows received on the origination of the liability, less any transaction costs.

Subsequently, any difference between the net cash flows and the residual value is recognised in profit or loss for the period using the effective interest rate method over the term of the liability. The financial liabilities reported by the Bank as deposits, borrowings and securities issued are stated at amortised cost.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument, or, where appropriate, a shorter period, to the present carrying amount of the financial asset or liability. When calculating the effective interest rate the Bank estimates cash flows considering all contractual terms of the financial instrument, but does not consider future credit losses. The calculation includes all charges and other fees paid to or received by the contractors that are an integral part of the effective interest rate.

Derecognition of financial instruments

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised when:

- a) the contractual rights to receive cash flows from the financial asset have expired;
- b) the contractual rights to receive cash flows from the financial assets have been transferred, or contractual rights to receive cash flows from the financial asset have been retained, but a contractual obligation has been assumed for their payment in full without material delay to a third party under a 'pass through' arrangement, and either:
 - the Bank has transferred substantially all the risks and rewards of the financial asset, or
 - the Bank has neither transferred nor retained substantially all the risks and rewards of the financial asset, but has transferred control of the asset.

When the Bank has transferred its contractual rights to receive cash flows from a financial asset and has neither transferred nor retained substantially all of the risks and rewards of the financial asset nor transferred control of the asset, the transferred financial asset is recognised to the extent of the Bank's continuing involvement in the asset. In this case, the Bank recognises the related obligation. The transferred asset and the concomitant obligation are evaluated to reflect the rights and obligations, which the Bank has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

A financial liability is derecognised from the separate statement of financial position when the obligation under the liability is discharged or cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts of the original and new liability is recognised in the separate statement of comprehensive income.

Impairment of financial instruments

A financial asset classified in Phase 1 – Standard (Performing) – is impaired individually on the basis of the probability of default of the debtor during the next 12 months or less, if the life of the instrument or the residual term is less than one year.

A financial asset classified in Phase 2 – Watch – is an asset for which there has not been a significant increase in credit risk since initial recognition. The Bank considers that there has been a significant increase in credit risk when contractual payments are more than 30 days past due; the debtor has been reclassified as watch exposure; the debtor's credit rating has deteriorated as at the reporting date compared to its rating as at the date of recognition of the instrument, or the Group expects that the credit will be restructured. In this case, the expected credit losses are calculated for the entire life of the asset.

A financial asset classified in Phase 3 – Non-performing – which is not recognised at fair value through profit and loss, is reviewed at each reporting date to assess whether there is objective evidence of its impairment. A financial asset is impaired when there is objective evidence that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows of the asset that can be estimated reliably.

Objective evidence a financial asset is impaired includes default or delinquency by a borrower, restructuring of a liability to the Bank on terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, adverse changes in the payment status of a borrower or issuer, economic conditions that lead to failures or the disappearance of an active market for a security.

Impairment of financial assets measured at amortised cost

The Group impairs assets on individual and collective bases. The Group considers evidence for impairment of financial assets measured at amortised cost (loans and receivables) at both individual and collective level.

Assets with similar risk characteristics are collectively assessed for impairment. In assessing collective impairment the Group uses historical trends of the probability of default, the timing of recoveries and the amount of loss incurred.

Impairment losses on financial assets measured at amortised cost are calculated as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Impairment losses are recognised in profit or loss and reflected in an allowance account against loans and advances or held-to-maturity investment securities. When an event occurring after the impairment was recognised causes the amount of impairment losses to decrease, the decrease in impairment loss is reversed through profit or loss.

Pursuant to the Policy and Rules for Calculation of Expected Credit Losses and Exposures Impairment, the understanding of the Bank and the Group of the impairment on a collective (portfolio) basis is as follows:

„Article 32. (1) Based on a motivated proposal by Risk Department, the bank may designate sub-portfolios of exposures with similar risk characteristics.

(2) The indicators underlying the establishment of a sub-portfolio are controlled and monitored at least once a year in order to identify potential unfavourable dynamics and changes in the risk profile of the portfolio.

Article 33. The amount of the collective impairment is determined in accordance with the methodology adopted by the Bank. It is also possible to develop additional methodologies that take into account specific risk factors for particular sub-portfolios.

Article 34. For groups of financial instruments the credit risk of which has increased significantly since initial recognition, a portfolio assessment can be made taking into account the information that shows a significant increase in credit risk at the level of a group or sub-group of financial instruments. Thus, the Bank recognizes expected credit losses over the entire life of financial instruments the credit risk of which has increased significantly, even when there is no such evidence at the level of an individual instrument.

Article 35. (1) When the Bank determines whether there has been a significant increase in credit risk and recognizes loss adjustments on a collective basis, financial instruments may be grouped on the basis of common credit risk characteristics with the aim to conduct an analysis to identify a significant increase in credit risk in a timely manner.

(2) By grouping its financial instruments, the Bank complies with the principle of not impairing the quality of information available by grouping financial instruments with different risk characteristics. Common characteristics of credit risk include, but are not limited to: a type of instrument; credit risk rating; type of collateral; date of initial recognition; residual term to maturity; industry; geographical location of the borrower; and the relative value of the collateral compared to the financial asset if it affects the probability of default (for example, non-recourse loans in some jurisdictions or loan / collateral ratios).“

Currently, the Group has designated as a portfolio for collective impairment its receivables on Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP).

For the Bank and the Group, *impairment on an individual basis* means (again, as defined in the same Policy) an assessment of the expected credit losses based on the exposure.s individual parameters.

1. When the exposure is in Phase 3, an individual matrix is applied to the expected future cash flows from collateral realisation.
2. When the exposure is in Phase 1 or 2, a tool is used to compare the exposure.s individual characteristics (such as maturity, payment models, sectors, etc.) with probabilities of non-performance, which have been observed historically with respect to similar exposures, as well as macroeconomic parameters, sector specifics, etc.

For financial assets comprising receivables under lease contracts, the expected credit loss is determined by cash flows compatible with cash flows used to measure the receivable under lease contract in accordance with IAS 17. The expected credit losses under lease contracts are discounted using the same discount rate which has been used to measure the lease receivables in accordance with IAS 17.

Impairment of assets measured at fair value through other comprehensive income

Impairment losses on financial assets measured at fair value through other comprehensive income are recognised by reclassification to profit or loss of the losses accumulated in the fair value reserve in the equity. The cumulative loss that is reclassified from equity to profit or loss is the difference between the acquisition cost, net of any principal repayments and amortisation, less any impairment loss previously recognised in profit or loss, and the present fair value.

Any changes in impairment attributable to the application of the effective interest method are reflected as a component of interest income. If, in a subsequent period, the fair value of an impaired debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognised, then

the impairment loss is reversed, with the amount of the reversal being recognised in profit or loss. An impairment is accrued for equity securities and every movement in the fair value is recognised in other comprehensive income until the security is sold or derecognised.

Fair value of financial assets and liabilities

Definitions

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Group discloses information about the fair value of those assets and liabilities for which there is market information available and the fair value of which significantly differs from their carrying amount.

The fair values of financial assets and liabilities that are quoted in active markets and for which there is market information available are based on announced market prices or closing prices. The use of real market prices and information reduces the need for management assessment and assumptions, as well as the uncertainty related to the determination of fair value. The availability of real market prices and information varies depending on products and markets, and changes according to the specific events and the general financial market conditions. For some of the other financial instruments the Group determines the fair values by using of an evaluation method based on the net present value. The net present value calculation is provided by market yield curves and credit spreads, where necessary, for the respective instrument. The purpose of evaluation techniques is to determine fair value, which would be priced by direct market participants. For investments in subsidiaries and associated companies, as well as for equity investments for which there are no observable market prices, the Group accepts that the fair value is the price of acquisition. The Group has an established control environment with respect to the assessment of fair values.

The fair values of financial instruments not traded in active markets (such as derivatives not traded on the market), which are an object of a transaction between the parties, are determined using valuation techniques. These valuation techniques adhere to the use of market data when available and as less as possible to the use of specific assessments of the entity.

Fair Value Hierarchy

The Group applies the following hierarchy for measuring and disclosing the fair value of financial instruments using valuation techniques:

- Level 1 – quoted (unadjusted) market prices in active markets for identical instruments;
- Level 2 – inputs other than quoted prices included within Level 1 that are observable either directly or indirectly. This category includes instruments valued using quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data;
- Level 3 – unobservable inputs for an asset or a liability. This category includes all instruments, for which the valuation technique does not include observable inputs and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments;

The fair value hierarchy of financial assets and liabilities is disclosed in Note 5.

Cash and cash equivalents

For the purposes of the cash flow statement cash equivalents comprise cash in hand, cash in current accounts with other banks, deposits and placements with other banks – payable at sight and/or with original maturity of up to 3 months, including repo deals with original maturity of up to 3 months, as well as unrestricted (not blocked) balances with the Central Bank (BNB). The parent company (the Bank) maintains a minimum statutory reserve according to the requirements of BNB and for the purposes of cash flow statement it includes these funds included as a component of Cash and cash equivalents.

They are presented in the separate statement of financial position at amortised cost.

For the purposes of preparation of the separate cash flow statement, bank overdrafts payable on demand and forming an integral part of the Group's cash management are included as a component of Cash and cash equivalents.

3.2 Other assets

Assets held for sale

Assets are classified as held for sale, if their carrying amount will be recovered through a sale and not through a continuing use in the Group's operations. Assets held for sale are stated initially at cost, with the transaction costs being taken into account in the initial measurement. Usually, these assets have been initially accepted by the Bank as collateral and subsequently acquired as a result of a "debt against property" exchange by borrowers that do not perform their obligations in accordance with the agreed contractual terms.

Assets classified in this group are available for immediate sale in their present condition.

Management is usually engaged actively and performs actions to realise a sale transaction within at least one year after the date of classification of the asset in this group.

Assets classified as held for sale are presented in the separate statement of financial position separately and measured at the lower of their carrying amount and their fair value less the estimated direct costs to sell.

The assets within this classification group are not depreciated.

Taxes

Current income taxes are determined by the Group entities in accordance with the Bulgarian legislation. The income tax due is calculated on the basis of the taxable profit for the period determined in accordance with the rules established by the tax authorities on the grounds of which taxes are paid (reversed).

The tax effect relating to transactions and other events reported in the separate statement of comprehensive income is recognised also in the separate statement of comprehensive income and the tax effect relating to transactions and other events reported directly in equity is also recognised directly in equity.

Deferred income tax liabilities are recognised for all taxable temporary differences, except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that at the time of the transaction affects neither the accounting profit nor taxable profit or (taxable loss).

Deferred income tax assets are recognised for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised except where the deferred income tax asset arises from the initial recognition of an asset or liability in a transaction that at the time of the transaction affects neither the accounting profit nor taxable profit or (loss).

Deferred taxes are recognised as income or expense, and are included in the net profit for the period, except in cases, when these taxes arise from transactions or events, reported for the same or another period directly in equity. Deferred taxes are charged to or deducted directly from equity, when they relate to items, which have been charged to or deducted from equity in the same or in a different period.

The Bulgarian tax law does not stipulate taxation on a consolidated basis.

Property, plant and equipment

Items of property, plant and equipment are presented on the separate financial statements at historical cost of acquisition, less any accumulated depreciation and impairment losses.

Initial recognition

Upon their initial acquisition, items of property, plant and equipment are valued at acquisition cost, which comprises the purchase price, including customs duties and any directly attributable costs of bringing the asset to working condition. Directly attributable costs include: costs for site preparation, initial delivery and handling costs, installation costs, professional fees for people involved in the project, non-refundable taxes etc.

Subsequent measurement

The approach chosen by the Group for subsequent measurement of property, plant and equipment, is the cost model under IAS 16 – acquisition cost less any accumulated depreciation and any accumulated impairment losses.

Any gain or loss on disposal of an item of property, plant and equipment (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised net in other operating income / expenses in profit or loss.

Depreciation method

The Group applies the straight-line depreciation method for property, plant and equipment. The useful life per group of assets is as follows:

- buildings – 50 years
- bank equipment and computers – 5 years
- motor vehicles – 5 years
- fixtures and fittings – 6.7 years

The useful life of the individual groups of assets is determined by the management considering: their physical wear and tear, features of the equipment, intentions for future use and expected obsolescence. The useful life of equipment is reviewed at each year-end and adjusted prospectively in case that any material deviations from future expectations concerning the terms of use are found. The useful life by groups was not changed compared to 2017.

Subsequent costs

Repair and maintenance expenses are recognised as current in the period in which they were incurred. Subsequent expenses relating to an item of property, plant and equipment that have the nature of replacement of certain components or improvements and restructuring are capitalised to the carrying amount of the relevant asset and its remaining useful life to the date of capitalisation is reassessed accordingly. At the same time, the

unamortised portion of replaced components is derecognised from the assets carrying amount and recognised as current expenses for the period of restructure.

Intangible assets

Intangible assets are presented on the separate financial statements at cost less accumulated amortisation and any accumulated impairment losses. They include software and software licences.

The Group applies the straight-line depreciation method for the intangible assets with a determined useful life of 5 years.

The carrying amount of the intangible assets is subject to review for impairment when events or changes in circumstances indicate that their carrying amount might exceed their recoverable amount. Impairment losses are recognised in the separate statement of comprehensive income.

Intangible assets are derecognised from the separate financial statement when permanently withdrawn from use (upon retirement), when no future economic benefits are expected from their use or on disposal. Any gains or losses on disposal of individual assets from the group of intangible assets are determined by comparing the sales proceeds and the carrying amount of the asset at the date of the sale.

Investment property

The Group's management uses this category upon lease of assets acquired from collateral foreclosure on loans. Investment property is measured initially at cost plus any transaction costs. Subsequent to initial recognition, investment property is recognised at fair value.

Any gain or loss due to changes in the fair value of investment property is recognised in the profit or loss in the period in which it has occurred. The fair value of investment property is determined on the basis of a valuation made by an independent appraiser.

Investment property rental income is presented as other operating income, while operating expenses directly or indirectly relating to the generated rental income are presented as other operating expenses. Investment property is derecognised on disposal or upon withdrawal from use (retirement), when no future economic benefits are expected from its disposal. Any gains or losses on derecognition of investment property are recognised in the profit or loss in the period in which they have occurred.

Assets acquired from collateral foreclosure

Assets acquired from collateral foreclosure are measured at the lower of cost and net realisable value in compliance with the requirements of IAS 2 Inventories.

Cost of the assets acquired from collateral foreclosure is the sum of all direct costs incurred on the acquisition of the assets and other expenses incurred on bringing them to their current location and condition. The net realisable value is the estimated selling price in the ordinary course of business less estimated costs to complete the trade cycle and costs to sell.

The impairment of these assets is calculated in accordance with the Group's accounting policy based on the expected realisation of the assets acquired from collateral foreclosure. The impairment of the assets acquired from collateral foreclosure is recognised in the statement of profit or loss. The Group's management is of the opinion that the carrying amount of the assets acquired from collateral foreclosure is the best estimate of their net realisable value at the date of the statement of financial position. The impairment of these assets as of 31 December 2018 amounts to BGN 0 (2017: BGN 0). Further details are provided in Note 26.

Impairment of non-financial assets

The carrying amounts of the Group's non-financial assets, other than investment property, inventory and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indications exist, then the asset's recoverable amount is estimated. For intangible assets with indefinite useful life or not yet brought into use, the recoverable amount is estimated annually. An impairment loss is recognised always when the carrying amount of an asset or a cash-generating unit (CGU) exceeds its recoverable amount.

An impairment loss is recognised always when the carrying amount of an asset or a cash-generating unit (CGU) exceeds its recoverable amount.

The recoverable amount of an asset or CGU is the greater of value in use and fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using the pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU. For impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGUs.

Impairment losses are recognised in profit or loss. Impairment losses recognised with respect to CGUs are allocated to reduce the carrying amount of the assets in the CGU on a pro rata basis.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised.

3.3. Liabilities

Financial liabilities, which are not derivative instruments or which have not been designated on acquisition as liabilities to be measured at fair value through profit or loss, are measured at amortised cost. Initially, they are stated at "cost", i.e. the fair value of cash flows received on the origination of the liability, less any transaction costs. Subsequently, any difference between the net cash flows and the residual value is recognised in profit or loss for the period using the effective interest rate method over the term of the liability. The financial liabilities reported by the Group as deposits, borrowings and securities issued are stated at amortised cost.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument, or, where appropriate, a shorter period, to the present carrying amount of the financial asset or liability.

When calculating the effective interest rate the Group estimates cash flows considering all contractual terms of the financial instrument, but does not consider future credit losses. The calculation includes all charges and other fees paid to or received by the contractors that are an integral part of the effective interest rate.

Financial assets and liabilities are offset and the net amount presented in the consolidated statement of financial position when, and only when, the Group has a legal right to set off the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

Pension and other payables to personnel under the social security and labour legislation

According to the Bulgarian legislation, the Group is obliged to pay contributions to social security and health insurance funds. The employment relations of the employees with the Group, in its capacity of an employer, are based on the provisions of the Labour Code.

Short-term employee benefits

Short-term employee benefits of the Group in the form of salaries, bonuses and social payments and benefits are recognised as an expense in the separate statement of comprehensive income in the period in which the respective service has been rendered or the requirements for their receipt have been met, and as a current liability at their undiscounted amount. The Group's obligations to make social security and health insurance contributions are recognised as a current expense and liability at their undiscounted amount together and in the period of accrual of the respective benefits they relate to.

At the end of each reporting period the Group assesses and reports the expected costs of accumulating compensated absences as the amount that is expected to be paid as a result of the unused entitlement. The assessment includes the estimated costs of employees remuneration and the statutory social security and health insurance contributions owed by the employer on these amounts.

Long-term retirement benefits

In accordance with the requirements of the Labour Code, the employer is obliged to pay to its personnel upon retirement an indemnity that depending on the length of service with the entity varies between two and six gross monthly salaries as of the date of employment termination. In their nature, these are defined benefit plans.

The calculation of the amount of these liabilities requires the involvement of qualified actuaries in order to determine their present value at the date of the separate financial statements, at which they are included in the separate statement of financial position, adjusted with the amount of the actuarial gains and losses, and respectively, the change in their value, including the recognised actuarial gains and losses – in other comprehensive income.

Past service costs are recognised immediately in the statement of comprehensive income in the period in which they were incurred.

At the end of each reporting period, the Group assigns certified actuaries who issue a report with calculations regarding the long-term retirement benefit obligations. For the purpose, they apply the Projected Unit Credit Method. The present value of the defined benefit obligation is determined by discounting the future cash flows, which are expected to be paid within the maturity of this obligation, and by applying the interest rates of long-term government bonds denominated in Bulgarian leva.

Actuarial gains and losses arise from changes in the actuarial assumptions and experience adjustments. Actuarial gains and losses from changes in demographic and financial assumptions upon retirement for assured length of service and age are recognised in the separate statement of comprehensive income.

Termination benefits

In accordance with the provisions of the Labour Code, the employer is obliged, upon termination of an employment contract prior to retirement, to pay indemnities as follows:

- for non-observed preliminary notice: one gross monthly salary;
- due to closing down the enterprise or part of it, outlays, reduction of the volume of work and work stoppage for more than 15 days, etc.: one gross monthly salary;
- upon termination of the employment contract due to illness: two gross monthly salaries;
- for unused annual paid leave: for the respective years of the time recognised as service period.

The Group recognises employee benefit obligations in the event of employment termination before the normal retirement date when it is demonstrably committed, based on an announced plan, to either terminating the employment of current employees without possibility of withdrawal or providing termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits falling due more than 12 months are discounted to and presented in the separate statement of financial position at present value.

Provisions and contingent liabilities

Provisions

Provisions are recognised when the Bank has a present legal or constructive liability as a result of past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the liability. Provisions are measured on the basis of the best management's estimate at the end of reporting period of the expenses necessary to settle the particular obligation. The estimate is discounted if the obligation is long-term.

Contingent liabilities

Contingent liabilities are obligations arising from past events, the existence of which can be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not entirely within the control of the Bank, or it is not probable that an outflow of resources will be required to settle the obligation. They are not recognised in the separate statement of financial position but are subject to special disclosure.

Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer of the guarantee to make specified payments to reimburse the holder as a result of the failure of a third party – debtor to comply with commitments made that have been guaranteed. Financial guarantee contracts are initially measured at fair value, whereas it is accepted that the guarantee's fair value on the date of its issuance is the premium received at inception. No receivables for the future premiums are recognized. Commission fee income is deferred on a straight-line basis over the period, to which such fees refer. Subsequently, the Group's liabilities under financial guarantee contracts are measured at the higher of the amount initially recognized less amortization and the provision that should have been accrued for the Group to meet its contractual obligations arising at the date of the financial statements. The expected credit losses, related to the financial guarantees issued, are recognised in the statement of comprehensive income, under the heading Impairment of financial assets. The likelihood of an obligation for payment by the Group under such contracts is estimated based on historical experience with similar instruments.

3.4 Capital

Share capital

The share capital is stated at the nominal value of shares issued and paid. Any proceeds from shares issued over their nominal value are reported as share premium.

Expenses directly relating to the issuance of new shares, except of such relating to business combinations are deducted from the capital net of any associated taxes. Dividends on ordinary shares are recognised in the period in which they were approved by the shareholders. Dividends for the period, which have been announced after the date of preparation of the financial statements, are disclosed as events after the date of the financial statements.

Dividends

An obligation for cash payables to the owners is recognised when the distribution has been approved by them and no longer depends on the Group. The corresponding amount is written off directly from equity.

3.5 Income and expenses

Interest income and interest expenses

Interest income and interest expenses are recognised in the statement of comprehensive income on an accrual basis for all interest-bearing instruments using the effective yield method based on the actual price of acquisition or the applicable floating interest rate. Interest income and interest expenses include the amortisation of any discount or premium, or any other differences between the original carrying amount of an interest-bearing instrument and its amount at maturity calculated on an effective interest rate (EIR) basis.

Interest income includes interest income on debt securities measured at fair value through other comprehensive income and through profits and losses, interest on deposits with other banks, interest on loans and advances to customers, and fees and commissions on loans and advances to customers, which are an integral part of the effective yield of the financial instrument.

Interest expense is recognised on an accrual basis and comprises the interest accrued on deposits of customers and banks, as well as on loans received and other borrowings, fees and commissions on loans received, which form an integral part of the effective interest expense.

For loans past due for more than 90 days, the balance sheet reporting of interest income, fee and commission income and other loan-related income is ceased. For exposures classified in Phases 1 and 2, the Group recognizes interest income and other EIR-forming income accrued on their amortised cost before the impairment for expected credit losses. For exposures classified in Phase 3, the Group recognizes interest income and other EIR-forming income accrued on their amortised cost less any impairment for expected credit losses.

The Group also holds investments and assets in countries with negative interest rate levels. The Group discloses the interest paid on such assets as interest expense with additional disclosure in Note 6.

Fees and commissions

Pursuant to IFRS 15 Revenue from Contract with Customers and the classification adopted, described in note 2.1, fee and commission income is recognized on a one-off or periodical basis over the life of the exposure, while ensuring comparability with the costs of providing the service, as well as consuming the benefits of the services provided by the customer.

Fee and commission expenses are recognised when the service, to which they relate, is provided or when the result thereof has been achieved.

Foreign currency transactions

Foreign currency transactions are translated into BGN at the exchange rate of BNB prevailing at the date of the transaction. Receivables and liabilities denominated in foreign currency are revalued on a daily basis. At the end of the year, they are translated in BGN at the closing exchange rates of BNB, which for the main currencies as of the date of the separate financial statements are the following:

Foreign currency	31 December 2018	31 December 2017
USD	1.70815	1.63081
Euro	1.95583	1.95583



Since 1999 the Bulgarian Lev (BGN) has been fixed to the Euro (EUR), the official currency of the European Union, at ratio of BGN 1.95583/ EUR 1.0

Net gains or losses on changes in exchange rates, which have incurred from revaluation of receivables, liabilities, as well as from foreign currency transactions, are presented on the separate statement of comprehensive income in the period in which they have occurred.

Segment reporting

The Bank does not report operating segments, because its major source of risk and return is the corporate business sector; there isn't a single external customer the revenue from whom to form more than 10 per cent of the total revenue, and the Group operates in the territory of the country. If these factors change in the future and the Group starts to report operating segments, they will be determined and presented in accordance with the requirements of IFRS 8 Operating Segments.

3.6 Cash and cash equivalents

For the purposes of the consolidated cash flow statement cash equivalents comprise cash in hand, cash in current accounts with other banks, deposits and placements with other banks – payable at sight (on demand) and/or with original maturity of up to 3 months, including repo deals with original maturity of up to 3 months, as well as unrestricted (not blocked) balances with the Central Bank (BNB). The parent company (the Bank) maintains a minimum statutory reserve according to the requirements of BNB and for the purposes of cash flow statement it includes these funds included as a component of Cash and cash equivalents.

They are presented in the consolidated statement of financial position at amortised cost.

For the purposes of preparation of the consolidated cash flow statement, bank overdrafts payable on demand and forming an integral part of the Group's cash management are included as a component of Cash and cash equivalents.

4. FINANCIAL RISK MANAGEMENT

In the ordinary course of business, the Group is exposed to a variety of risks that, if occur, could result in formation of losses and deterioration of the Group's financial stability. These risks are identified, measured and monitored through various control mechanisms in order to be managed and to prevent undue risk concentration. The process of risk management is essential for the Group's profitability and existence.

The risk management within Bulgarian Development Bank Group is a complex of methods and procedures used by the Group for identifying, measuring and monitoring its risk exposures. The Group manages the following main categories of risk:

- Credit risk;
- Liquidity risk;
- Market risk;
- Operational risk.

When managing the risks, the Group applies policies and procedures relevant to the nature and complexity of its activity, which are based on best practices in banking industry.

Risk management structure

The main units that are directly responsible for risk management are as follows:

For the parent company (the Bank):

- *Supervisory Board* – performs overall supervision of risk management;
- *Management Board* – responsible for the overall risk management approach and for approving risk management strategies, principles and specific methods, techniques and procedures;
- *Risk Committee* – responsible for exercising control over the implementation of the risk management policies by various types of risk, as well as the adequacy of the Bank's risk profile to the tasks assigned to it.
- *Committee on Assets and Liability Management (ALCO)* – responsible for the strategic management of assets and liabilities and for market risk management, including liquidity risk management, related to the assets and liabilities.
- *Provisions Committee* – analyses credit transactions from the perspective of credit risk management for the loan portfolio in general, as well as of the level of credit deals and borrowers;
- *Executive Directors and members of the Management Board* – exercise current operating control of the maintenance and monitoring of the limits set for a particular types of risk and the application of the established procedures.
- The Central Bank exercises supplementary supervision of risk management by requiring periodically regulatory reports and exercising subsequent control on the compliance with the statutory maximum levels of exposure to certain risks.

For the subsidiary National Guarantee Fund (the Fund)

The main units responsible for the management of risks are:

- *Supervisory Board* – Management Board of BDB AD (the parent company) – performs overall supervision of risk management;
- *Board of Directors* – responsible for the overall approach towards risk and approves risk management strategies, principles and specific methods, risk management techniques and procedures;
- *Provisions Committee* – analyses the guaranteed portfolio in terms of overall credit risk management of the whole portfolio, as well as of each guarantee deal and each beneficiary of the guarantee itself.
- *Risk and Monitoring Department* – performs monitoring of the guaranteed portfolios and the collateral provided. At least annually an inspection over the fulfilment of the economic and social requirements for the SME using a guarantee from National Guarantee Fund EAD is carried out.

For the subsidiary Microfinance Institution “JOBS” EAD (MFI):

The main units responsible for the risk management are:

- *Board of Directors* – responsible for the adoption of risk management rules and procedures; exercising control over the risk factors of the Company and making decisions within their powers; as well as for conducting analyses of all credit transactions exceeding BGN 100 thousand in view of credit risk management upon their approval;
- *Credit committee* – monitors and analyses on an ongoing basis the loan and lease portfolio of the Company in terms of credit risk, including by individual transactions;
- *Credit Council* – analyses credit and leasing transactions in terms of credit risk management upon their approval and / or renegotiation;
- *Operational Management (Executive Director and Deputy Executive Directors)* – organises the activities for the implementation of the Rules for Risk Management adopted by the Board of Directors; creates a work organisation that ensures compliance with the limits and risk levels set; exercises control over the compliance of the risk analysis, measurement and evaluation procedures with the internal documents adopted by the Board of Directors;
- *Risk Management Department* – develops and implements a risk management system; prepares and submits to the Board of Directors periodic reports for assessing the operational risks, including the observance of the limits, and reports on an ongoing basis to the Operational Management of the Company; performs initial and ongoing validation of the risk assessment methods; examines the inputs needed for the risk assessment in accordance with applicable principles of reliability and sufficiency.

For the subsidiary Capital Investment Fund AD:

At present, CIF carries out no activity.

For the subsidiary TC Maritsa EOOD:

The risk management functions are exercised by the operational units – General Manager and Chief Accountant. The activity of TC Maritsa does not include financial assets acquisition and management.

Measurement and management of major risks

Management of the Group companies has adopted a set of internal rules and procedures for measuring various risks, which are based on statistical models and best international banking practices, as well as on the historical experience of the Group itself.

Risk monitoring and management are primarily based on limits. Those limits reflect on the Group's strategy and its market position, as well as on the level of risk that can be borne. Reports on the specific types of risks are periodically prepared for the purpose of subsequent analysis and possible adjustments of already set limits.

4.1. Credit risk

Credit risk is the risk of potential losses due to a failure of the Group's customers to discharge their contractual obligations in connection with receivables and financial instruments held by the Group, incl. country (sovereign) risk, contractor's risk and settlement risk, and credit risk of concentration.

Credit risk is the main risk for the Group and therefore, its management is fundamental for its activity. Credit risk management is performed in accordance with the Bulgarian Development Bank Act (the parent company) and the effective laws and regulations of the Republic of Bulgaria regulating credit activity, as well as the international regulations and best banking practices, and the requirements of IFRS.

In assessing and managing credit risks (including the counterparty risk) of its exposures, the Group applies internal rating generation models. These internal rating models depend on the specifics of the object being rated.

The so-developed rating models for credit risk assessment of corporate clients of the Bank are based on an analysis of historical data and the counterparty's and its relating parties. current financial position; their history and behaviour in servicing their liabilities to other contractors; future cash flow analyses; sources of servicing the existing and any potential future liabilities to the Group, and other parameters specific to a particular transaction. Credit portfolio quality monitoring, control and assessment units are established and function within BDB. Credit portfolio current monitoring, reporting and management procedures and mechanisms are implemented, which require periodical, and if necessary, extraordinary, reports on the financial and credit status of each borrower and other liable persons. There is an „Early Warning Procedure for Corporate Credit Clients“, which includes an early warning system of signals and actions.

In managing its credit risk, the Group applies an intra-bank system of limits that is subject to periodic review and updating.

Within the Group, there is an Impairment and Provisions Committee (IPC) that participates in the credit risk management and is in charge of the assessment of quality and classification of exposures, holds monthly meetings and reports to the Management Board of the parent company.

There is a specialized unit functioning within the Group, which is in charge of the risk assessment both at the customer level and at the exposure level, where the solvency level is assessed and monitored throughout the entire loan term – from application to full repayment. The credit risk is partially reduced also by accepting different types of collateral, where at any point in time the valuation of collateral shall not be older than 12 months.

Following a decision of the Provisions Committee, the Group forms impairment on exposures both at an individual and collective basis depending on the borrower's risk profile.

The exposures in the Group's corporate credit portfolio are classified mainly in three categories depending on the existence of indications of impairment – changes in the objective indicators on the basis of which the initial measurement and subsequent monitoring of exposure / customer are carried out, which would result in changes in cash flows from financial assets, including default in payment due by the borrower: Phase 1 „Standard“ (with assigned internal credit ratings from 1 to 6, incl.; Phase 2 “Watch” or “Forborne” (with assigned internal

credit ratings of 7 or 8) and Phase 3 „Problematic/non-performing“ (with assigned internal credit ratings of 8, 9 or 10). In the case of customers, for which there are currently no indications of increased risk, the Group periodically (at least once a year) reviews the financial and legal status, including the collateral accepted, in order to establish the need for a change in the percentage of impairment for loss risk and / or change in the assessment of the degree of credit risk. Clients with a higher credit risk are subject to a review in every 6 months and those classified as „problematic/non-performing“, in every three months.

In the case of customers, for which there are currently no indications of increased risk, the Group periodically (at least once a year) reviews the financial and legal status, including the collateral accepted, in order to establish the need for a change in the percentage of impairment for loss risk and / or change in the assessment of the degree of credit risk. Clients with a higher credit risk are subject to a review in every 6 months and those classified as „problematic/non-performing“, in every three months. In follow-up of the recommendations of the Basel Committee and their transposition into regulations within the European Union and in particular, Regulation 575/2013/EU and Directive 2013/36/EU, the commercial banks are required to implement in their internal regulations an in-house rating system that allows them to achieve comparability with the borrowers. Official crediting rating assigned by recognized external credit rating institutions, which adopts the scale, used worldwide, of ten credit rating categories, including two categories for non-performing loans.

The Group has developed a detailed internal set of policies, rules and procedures, comprising Policy and rules for determining the impairment due to uncollectability of risk exposures, Methodology for credit risk analysis and assessment of Bulgarian Development Bank AD, and Credit activity manual of BDB, ensuring full compliance of the policy and procedures for determining internal credit ratings with the above quoted EU regulations. The amount of the impairment is calculated as the difference between the current amount of the amortised cost of the customer's exposure to the Group and its recoverable amount.

The Group accrues impairment on a portfolio basis for its receivables on the EEMFBNP.

Aiming at minimizing and reducing the credit risk, the Group accepts collateral in accordance with its in-house rules. It is a common practice of the Group to require collateral from the borrowers that is equal to at least 100 per cent of the agreed loan amount, and valuations from accredited independent valuers are required.

Based on a Guarantee letter from year 2003 and the subsequent annexes signed with the European Investment Fund (EIF), the parent company (the Bank) participates in the EU SME Guarantee Facility under conditions determined by the long-term EU Program on SMEs. EIF is committed to provide a direct guarantee covering 50 per cent of the remaining loss on the principal and interest of each loan, included in the sub-portfolio of the Bank, formed on the basis of the conditions of the agreement, but not exceeding EUR 2,520 thousand (BGN 4,929 thousand). The Bank has applied reduced requirements in accepting collaterals for the EIF-guaranteed portfolio of loans. As of 31 December 2018, the total exposure on EIF-guaranteed loans amounted to BGN 5,286 thousand (31 December 2017: BGN 5,659 thousand). This amount includes the utilised but not yet repaid portion of the loans, as well as the Bank's commitments on unutilised loans. The payment engagement of EIF to date amounts to BGN 3,563 thousand (31 December 2017: BGN 3,563 thousand), whereas the losses covered by EIF amount to BGN 2,617 thousand (31 December 2017: BGN 2,773 thousand).

In November 2016, the parent company (the Bank) signed a counter-guarantee agreement with the European Investment Fund (EIF) under the COSME programme for small and medium-sized enterprises. The COSME programme is implemented with the support of EFSI (the European Fund for Strategic Investment), known as the „Juncker Plan“. The parent company (the Bank) is able to cover up to 60 per cent of the risk on loans extended to SMEs by commercial banks it will partner with. Half of this risk will be counter-guaranteed by EIF and the total amount of the counter-guarantee is EUR 10 million. By using the resource guaranteed by the COSME programme, the banks-partners to the parent company (the Bank) will be able to extend investment loans and loans for working capital, bank guarantees and revolving loans. The maximum amount of loans extended is EUR 150,000. The term of repayment vary from 1 to 10 years.

As at 31 December 2018, there was no commitment on the counter-guarantee agreement.

Off-balance sheet commitments, primarily the unutilised portion of authorized loan facilities, letters of guarantee and letters of credit, which represent an irrevocable commitment of the Group to make payment if a client is not able to fulfil its obligations to third parties represent another source of credit risk for the Group and bear the same credit risk as the loan exposures.

The parent company (the Bank) forms various sub-portfolios based on the type of contractors and credit risk carriers, as following:

- Direct lending – portfolio of credit commitments with debtors-legal entities, other than bank financial institutions, and loans to individuals (loans to Bank.s employees), as well as subjects from the public sector;
- Indirect lending or „on-lending“ – portfolio of loans to financial (banking and non-banking) institutions, the purpose of which is to provide financing/to facilitate the access to financing for micro, small and medium-sized enterprises in the Republic of Bulgaria;
- Financing by the National Programme for Energy Efficiency of Multi-Family Residential Buildings in compliance with CMD 18 of the CoM.

Beyond the credit portfolio, the Group.s activity is exposed to credit risk also with respect to exposures related to other activities of the Group:

- portfolio of financial instruments, other than loans, formed in connection with the Group.s free cash management, which comprises mainly government securities issued by the Republic of Bulgaria, classified as „ Financial assets at fair value through other comprehensive income “;
- to banks in connection with money market transactions, placed term deposits and available balances in Nostro accounts;
- receivables relating to the State budget.

The Group applies a system of limits relating to credit risk and concentration risk with respect to the different sub-portfolios, and currently monitors the credit risk of concentration of financial assets on the basis of industry criteria, and also by individual counterparty, and insurance companies ensuring coverage. Regarding the Group’s direct credit portfolio, the allocation by economic sectors is monitored, as also that to clients and groups of related parties, by observing internal limitations (limits) for concentration of the corporate credit portfolio by economic sectors.

Maximum exposure to credit risk

Exposure to credit risk attributable to financial assets recognised in the consolidated statement of financial position is as follows:

Financial asset	2018		2017	
	maximum	net	maximum	net
Cash in Central Bank	297,622	297,622	447,648	447,648
Receivables from banks	431,119	431,119	198,910	198,910
Loans and advances to customers	1,211,190	1,144,631	867,086	775,171
Receivables from the State budget	472,803	472,803	737,516	737,516
Net investment in finance lease	1,418	1,418	1,035	1,035
Available-for-sale securities	-	-	291,867	291,867

	2018		2017	
Financial assets at fair value through other comprehensive income	653,657	653,657	-	-
Securities held to maturity	-	-	594	594
Securities at amortised cost	10,216	10,216		
Other financial assets	908	908	727	727
	3,078,933	3,012,374	2,545,383	2,453,468

The amount in the net amount of “Loans and advances to customers” is presented net of highly liquid collateral.

The heading Receivables from the State Budget comprise loans on the Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP) amounting to BGN 471,999 thousand (2017: BGN 728,010 thousand).

The exposure to credit risk attributable to off-balance sheet contingent commitments is as follows:

	2018		2017	
	maximum	net	maximum	net
Guarantees and letters of credit	484,134	468,595	407,746	398,274
Unutilised amount of authorized loans	328,324	328,324	446,223	446,223
Participation in the SIA investment program	1,410	1,410	1,603	1,603
	813,868	798,329	855,572	846,100
Maximum exposure to credit risk	3,892,801	3,810,703	3,400,955	3,299,568

In assessing the net exposure, highly liquid collateral (government securities and cash), as also the net present value of liquid collateral – real estate, have been taken into account.

Credit risk – concentration

The biggest credit exposure of the Group to a group of related parties /other than bank institutions/ amounts to BGN 149,182 thousand (2017: BGN 67,947 thousand) at amortised cost, which represents 19.96 per cent of Group’s equity. The concentration of client.s portfolio (other than bank institutions) is presented in the following table:

	2018		2017	
	(BGN.000)*	% of equity	(BGN.000)*	% of equity
The biggest total exposure to a customer group	149,182	19.97%	67,947	9.19%
Total amount of the ten biggest exposures	706,117	94.54%	382,844	51.77%
Total amount of the twenty biggest exposures	997,126	133.50%	715,721	96.78%

*The amount of the exposure net of impairment and highly liquid collateral.

There is no exposure to a customer or a group of related customers as at 31 December 2018, exceeding 25 per cent of Group’s capital base.

The financial assets of the Group, classified by industry sectors, are presented in the table below. Loans and receivables, as also finance leases are stated at amortised cost before impairment:

Sectors	2018	%	2017	%
Government	1,150,029	37.35	1,058,773	40.40
Financial services	850,433	27.62	718,994	29.43
Construction	162,762	5.29	146,790	5.93
Transport	131,778	4.28	106,835	4.28
Industry, total	484,815	15.74	304,023	12.17
<i>Industry – energy generation and distribution</i>	120,029	3.90	85,437	3.44
<i>Industry – other industries</i>	96,654	3.14	47,039	1.78
<i>Industry – manufacture of foodstuffs</i>	51,392	1.67	50,032	2.03
<i>Industry – manufacture of tobacco products</i>	149,129	4.84	58,773	2.38
<i>Industry – manufacture of plant and equipment</i>	67,611	2.20	62,742	2.54
Trade	34,571	1.12	39,005	1.45
Administrative and office activities	253	0.01	49,342	1.98
Other industries	66,596	2.16	12,476	0.28
Real estate transactions	49,741	1.62	49,475	2.00
Agriculture	34,817	1.13	33,905	1.09
Tourist services	108,948	3.54	17,366	0.66
Collection and disposal of garbage	4,190	0.14	8,399	0.34
	3,078,933	100.00	2,545,383	100.00

Quality of loans and receivables

The structure of the financial assets of the Group by risk classification groups is as follows (at amortised cost before impairment):

As of 31 December 2018	Standard (Phase 1)	Watch (Phase 2)	Non- performing (Phase 3)	Total
Cash in hand and balances in current account with the Central Bank	297,622	-	-	297,622
Receivables from banks	431,119	-	-	431,119
Loans for commercial property and construction	257,036	70,797	66,661	394,494
Trade loans	252,676	72,842	116,503	442,021
Agricultural loans	-	-	2,040	2,040
Consumer loans	778	-	19	797
Residential and mortgage loans to individuals	1,436	-	-	1,436

As of 31 December 2018	Standard (Phase 1)	Watch (Phase 2)	Non- performing (Phase 3)	Total
Loans to other financial institutions	63,107	-	44,661	107,768
Other loans and receivables	128,382	93,833	40,419	262,634
Net investment in finance lease	632	225	561	1,418
Receivables from the State budget	472,803	-	-	472,803
Financial assets at fair value through other comprehensive income	653,657	-	-	653,657
Securities at amortised cost	10,216	-	-	10,216
Other financial assets	908	-	-	908
Total financial assets	2,570,372	237,697	270,864	3,078,933

At 31 December 2017 (restated)*	Standard (Phase 1)	Watch (Phase 2)	Non- performing (Phase 3)	Total
Cash in hand and balances in current account with the Central Bank	447,648	-	-	447,648
Receivables from banks	198,910	-	-	198,910
Loans for commercial property and construction	267,005	73,965	65,651	406,621
Trade loans	217,368	10,137	114,604	342,109
Agricultural loans	-	-	2,103	2,103
Consumer loans	900	28	-	928
Residential and mortgage loans to individuals	1,972	-	-	1,972
Loans to other financial institutions	24,767	-	44,541	69,308
Other loans and receivables	21,666	667	21,254	43,587
Net investment in finance lease	981	63	449	1,493
Receivables from the State budget	737,516	-	-	737,516
Available-for-sale securities	291,867	-	-	291,867
Securities held to maturity	594	-	-	594
Other financial assets	727	-	-	727
Total financial assets	2,211,921	84,860	248,602	2,545,383

* Following the entry into force of IFRS 9, the Group conducted a review of its exposures and their internal credit rating and made them compliant with the standards requirements. Until 31 December 2017, part of exposures with credit rating of 8 were classified as „Watch“ in accordance with IAS 39. Since 1 January 2018, the loan assigned a rating of 8 have been classified in Phase 3 only. As a result, exposures with gross amount of BGN 70,476 thousand and an internal rating of 8 have been classified in Phase 3 („Non-performing“).

The table below presents the types of collaterals, received by the Bank in relation to loans granted, at fair value determined by accredited independent valuers and confirmed by a Bank's employee holding the necessary licence:

Type of collateral	2018		2017	
	Fair value	%	Fair value	%
Mortgages	514,012	52.31	252,215	42.18
Mortgages on ships	148,321	15.09	111,711	18.68
Pledges of plant, machinery, equipment, and inventories	273,290	27.81	213,538	35.71
Restricted deposits	4,164	0.42	3,176	0.53
Credit risk insurance	18,482	1.88	16,237	2.72
Bank guarantees	3,863	0.39	1,064	0.18
Securities quoted on an exchange	20,536	2.09	-	-
Total collateral	982,668	100.00	597,941	100.00

Credit exposures could have more than one collateral, i.e. it could be included in more than one position. The amount of the collateral could exceed 100 per cent, as more than one collateral could be provided to secure one loan.

At the request of the contractors, the Bank is able to re-negotiate the initial terms and conditions on the contract. Usually, these are the terms of loan utilization, loan amount, interest rates and/or repayment schedules from the point of view of the amount of a particular repayment instalment. Most of all, these are cases of changes in the initial parameters, purpose and scope, and respectively, the time schedule of projects. Upon renegotiation, the changes in preliminary terms and conditions are analysed in order to establish whether these changes represent a concession (discount) in favour of the debtor and the exposure should be accepted as restructured and therefore, to be reclassified to Phase 2 or Phase 3 pursuant to the Policy and Rules for Calculation of Expected Credit Losses and Exposures Impairment of BDB, which is applied by the other Group entities, as follows:

„Article 11. Indicators of impairment :

(1) Significant increase in credit risk, which results in recognition of a lifetime expected credit loss for the instrument (i.e. transition from a 12-month expected credit loss) and respectively, classification in Phase 2 (Watch) would be a consequence of the following circumstances:

1. significant changes in internal credit risk indicators as a result of a change in credit risk relative to the beginning of the life of the asset;

2. other changes in interest rates or the conditions of an existing financial instrument that would be materially different if the instrument was newly granted or issued at the date of the financial statements (for example, more stringent terms and conditions, increased collateral or warranty requirements) due to changes in the credit risk of the financial instrument compared to that of its initial recognition;

3. significant changes in the external market indicators of credit risk for a particular financial instrument or similar financial instruments with the same life expectancy. Changes in credit risk margins include, but are not limited to:

a) credit spread;



- b) *the credit default swap price for the borrower;*
 - c) *duration of the period or the extent to which the fair value of a financial asset is lower than its amortized cost; and*
 - d) *changes in the price of borrower.s debt and equity instruments;*
 - e) *any other market information about the borrower.*
4. *actual or expected significant change in the financial instrument's external credit rating (or of the debtor);*
 5. *actual or expected downgrade of the borrower's external credit rating or a downgrade in the scoring rating used to measure credit risk;*
 6. *existing or expected adverse changes in business, financial or economic conditions, for which it is expected to result in a significant change in the borrower.s ability to perform its obligations.*
 7. *actual or expected significant change in the borrower's operating results, such as actual or expected decreasing revenue or margins, increase in operating risks, working capital shortage, asset quality deterioration, increased leverage, low liquidity, management problems or changes within the scope of business or organisational structure that results in a significant change in the borrower's ability to perform its obligations on the debt;*
 8. *significant increases in credit risk for other financial instruments of the same borrower;*
 9. *actual or expected significant adverse change in the borrower's regulatory, economic or technological environment, which has resulted in a significant change in the borrower's ability to perform its obligations;*
 10. *significant changes in the value of the debt collateral or in the quality of guarantees and additional credit protection provided by a third party that are expected to reduce the economic incentive of the borrower to make scheduled contractual payments or to otherwise impact on the probability of default on the loan;*
 11. *significant change in the quality of a guarantee provided by a shareholder (or by the owner of an entity) if the shareholder (owners) have an incentive and financial opportunity to prevent default through an increase in capital and / or cash;*
 12. *significant changes, such as a reduction in financial support from a parent company or other subsidiary, or actual or expected significant change in the quality of credit protection that is expected to reduce the economic incentive for the borrower to make contractual payments.*
 13. *expected changes in the loan documentation, including an expected breach of the contract, which may lead to the debtor being released from the obligation to comply with contractual commitments or amendments to the contract, interest rates, interest rate increases, requirements for additional collateral or guarantees, or other changes in the contractual framework of the instrument;*
 14. *significant changes in the expected results and behaviour of the borrower, including changes in the creditworthiness of the borrowers within the group;*
 15. *specific changes in the Bank's approach for managing the loan in relation to the financial instrument; for example on the basis of newly emerging indicators of a change in financial instrument's credit risk, it is expected that the Bank's credit risk management practice will become more active or focused on instrument management, including more prudent or stringent monitoring, or active intervention in the relationships with the borrower;*
 16. *information on arrears, including cases of amounts past due by more than 30 days (if there is evidence that a significant number of defaulting debtors for more than 30 days have not reached the stage*



of significant deterioration, this threshold may be increased; however, extensive supporting data will be required in accordance with the provision of paragraph B5.5.19 of IFRS 9);

17. initiation of court proceedings; claiming of bank guarantees or other circumstances that are expected to result in significant costs for the borrower;

18. considerable delay in the provision by the borrower of financial and other necessary information;

19. undertaking of significant obligations of the borrower towards third parties, incl. off balance sheet, which would result in difficulties or inability to properly service the Bank's credit exposure.

(2) Events related to a classification where a financial instrument is classified in Phase 3, i.e. it is considered to be an asset with deteriorated credit quality and which, in most cases, correspond to the definition of default on the instrument, include:

1. significant financial difficulties of the debtor;

2. past due or unpaid liabilities to the Bank for more than 90 days;

3. provision of a concession to the debtor in view of its financial difficulties, which would otherwise not have been provided by the Bank;

a) if, as a result of the re-negotiation and provision of a concession to the debtor resulting in changes of cash flows the asset is derecognised and a new one is created (initially recognised), the Bank estimates only the 12-month expected loss. Further analysis of the expected credit loss is carried out if an increased credit risk exists.

b) if, a result of the re-negotiation and provision of a concession to the debtor resulting in changes of cash flows the asset is derecognised and a new one is created (initially recognised), but as a consequence the latter is reported as an impaired asset acquired / occurred, the Bank recognises the cumulative changes in the expected credit losses over its entire life.

c) if, a result of the re-negotiation and provision of a concession to the debtor, the financial asset is not derecognised, the Bank analyses whether there is a significant increase in credit risk, comparing:

(aa) the risk of default assessed at the reporting date (based on changed contractual terms); and

(bb) the risk of default assessed at initial recognition (on the basis of the original unchanged contractual terms);

in order to establish whether it should recognise lifetime expected credit losses or 12-month expected credit losses;

4. high probability of insolvency of the debtor or other financial reorganization of the debtor;

5. other evidence of deterioration in the debtor's creditworthiness."

Regarding the loans extended under the Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP), it should be noted that according to the programme's parameters the amount of the loan approved is subject to regular updating in order to ensure expenditure control. The signature of annexes to the loan contracts, by means of which the financial parameters are updated, is a result of those controls.

The table below presents data on the portfolio amount of the Group's financial assets by type of instrument at amortised costs and the accumulated impairment losses:

	Loans and receivables from non-financial institutions	Receivables from the State budget	Loans and receivables from financial institutions	Loans and receivables from individuals	Cash in hand and balances in current account with the Central Bank	Financial assets carried at fair value through other comprehensive income	Financial assets, held for trading	Securities held to maturity	Net investment in finance lease
At 31 December 2018									
Impaired on an individual basis									
----standard (Phase 1)	700,338		98,971	2,214		574,099			632
----watch (Phase 2)	235,445	-	1,467	-	-	-	-	-	225
----non-performing (Phase 3)	256,589	-	-	19	-	-	-	-	561
Gross amount	1,192,372	-	100,438	2,233	-	574,099	-	-	1,418
<i>Incl. renegotiated</i>	890,548	-	48,290	-	-	-	-	-	-
Past due but not impaired									
---standard (Phase 1)	-	-	-	-	-	-	-	-	-
---watch (Phase 2)	1,502	-	-	-	-	-	-	-	-
---non-performing (Phase 3)	9,746	-	-	-	-	-	-	-	-
Gross amount	11,248	-	-	-	-	-	-	-	-
<i>Incl. renegotiated</i>	10,089	-	-	-	-	-	-	-	-
Within 30 days	3,389	-	-	-	-	-	-	-	-
From 30– 90 days	852	-	-	-	-	-	-	-	-
Over 90 days	7,007	-	-	-	-	-	-	-	-
Impaired on a portfolio basis									
-----standard	-	472,803	-	-	-	-	-	-	-
Gross amount	-	472,803	-	-	-	-	-	-	-
Incl. renegotiated	-	-	-	-	-	-	-	-	-
Not past due and not impaired									
-----Phase 1	874	-	330,222	-	297,622	79,558	-	10,216	-
-----Phase 2	526	-	-	-	-	-	-	-	-
-----Phase 3	3,949	-	-	-	-	-	-	-	-
Gross amount	5,349	-	330,222	-	297,622	79,558	-	10,216	-
Incl. renegotiated	5,337	-	48,290	-	-	-	-	-	-
	1,208,969	472,803	430,660	2,233	297,622	653,657	-	10,216	1,418
Gross amount	905,974	-	48,290	-	-	-	-	-	-
Incl. renegotiated									

	Loans and receivables from non-financial institutions	Receivables from the State budget	Loans and receivables from financial institutions	Loans and receivables from individuals	Cash in hand and in current account with CB	Available-for-sale securities	Financial assets held for trading	Securities held for maturity	Net investment in finance lease
At 31 December 2017									
Impaired on an individual basis									
-watch	78,875	-	-	28	-	-	-	-	63
-non-performing	151,955	-	-	-	-	-	-	-	449
Gross amount	230,830	-	-	28	-	-	-	-	512
Incl. renegotiated	177,625	-	-	-	-	-	-	-	-
Past due but not impaired									
- standard	46,280	-	-	-	-	-	-	-	-
- watch	33,295	-	-	-	-	-	-	-	-
- non-performing	23,325	-	-	-	-	-	-	-	-
Gross amount	102,900	-	-	-	-	-	-	-	-
Incl. renegotiated	65,290	-	-	-	-	-	-	-	-
Within 30 days	51,710	-	-	-	-	-	-	-	-
From 30– 90 days	17,269	-	-	-	-	-	-	-	-
Over 90 days	33,921	-	-	-	-	-	-	-	-
Not past due and not impaired									
- standard	424,885	737,516	198,910	2,872	447,648	291,867	-	594	981
- watch	101,062	-	-	-	-	-	-	-	-
- non-performing	4,509	-	-	-	-	-	-	-	-
Gross amount	530,456	737,516	198,910	2,872	447,648	291,867	-	594	1,493
Incl. renegotiated	360,961	-	66,269	494	-	-	-	-	-
Gross amount	864,186	737,516	198,910	2,900	447,648	291,867	-	594	1,493
Incl. renegotiated	603,876	-	66,269	494	-	-	-	-	-

Loans with carrying amount that is lower than the amount of the valid collateral provided are included under heading „Past due but not impaired“.

The Bank classifies not past due and not impaired exposures to the above classes depending on their internal credit rating, as follows:

- high class – credit rating from 1 to 3 – Phase 1
- standard class – credit rating from 4 to 5 – Phase 1
- low class – credit rating from 6 to 7 – Phase 1 (rating 6) or Phase 2 (rating 7)
- non-performing – Phase 3 (rating 8, 9 and 10)

The Bank assesses the credit quality of provided contingent commitments by applying a methodology, which estimates whether events indicating with a high probability that outflow of Bank's resources might take place have occurred. These costs (losses) are determined on the basis of the Policy and Methodology for assessment of expected credit losses, and a Calculation Procedure of BDB based on a Conversion Factor (CCF) that is applied in the case of off-balance sheet exposures that are likely to turn into balance sheet exposures (payments on guarantees, utilisation of part of the allowed amount of the loan, etc.).

At the date of the financial statements, the Group identified commitments amounting to BGN 484,134 thousand (2017 : BGN 407,746 thousand), which were provided by BGN 7,641 thousand (2017: BGN 5,829 thousand) (Note 31).

Watch loans and receivables (Phase 2), presented at amortised cost, are as follows:

	2018	2017
Loans for commercial property and construction	70,797	84,936
Trade loans	72,842	52,873
Consumer loans	-	28
Other loans and receivables	93,834	17,499
Loans to banks	1,467	-
	238,940	155,336

When the initial terms of the agreement have been modified by the parent-company (the Bank) by granting a concession (discounts) to a debtor experiencing difficulties in performing its financial obligations a loan is classified as "restructured".

The restructured loans and receivables, presented at amortised cost, are as follows:

In BGN'000	2018	2017
Loans for commercial property and construction	47,387	56,955
incl. Performing – Phase 1	966	5,443
Watch – Phase 2	9,412	14,068
Non-performing – Phase 3	37,009	37,444
Other loans and receivables	67,315	67,867
incl. Performing – Phase 1	-	53,330
Watch – Phase 2	52,971	1,548
Non-performing – Phase 3	14,344	12,989
	114,702	124,822

Expected credit losses (ECL) reporting

For instruments measured at amortised cost, ECLs reduce the carrying amount in the statement of financial position.

For debt instruments measured at fair value through other comprehensive income, ECLs are part of the negative change in the fair value due to an increased credit risk. They continue to be presented at the fair value in the statement of financial position, and the accumulated adjustment for losses is recognized in the statement of comprehensive income. Upon subsequent derecognition of the instrument, the accumulated adjustment is recognized in the profit or loss for the period.

Risk parameters affecting (ECL)

Probability of default (PD)

PD is the probability of a counterparty not complying with contract clauses related to debt repayment. For each individual exposure or a portfolio of collectively assessed exposures, the Group maintains historical information on the migration of exposures between different phases.

The value of 12M PD is determined on the basis of observed deterioration rates and is calculated as a moving average over a period of at least 2 years. For exposures that are individually measured, the value of the 12m PD is determined depending on the assigned credit rating according to an internal model. Data on the changes in the borrowers' rating over a one-year horizon is aggregated into transaction matrices, and a 12-m PD is calculated for each rating scale depending on the number of default cases found. The Group adjusts the values of 12m PD to reflect the current or expected economic conditions that may differ from those during the historical periods analysed.

Exposure at default (EAD)

EAD is potential exposure at the time of default. The level of exposure at default is determined individually for each loan depending the type of loan, taking into account both the amount of utilized amounts and the agreed undrawn amounts according to the expectation of future drawdowns.

Loss Given Default (LGD)

LGD is the ratio of the exposure loss due to default to the amount of exposure at default. The Group calculates the potential loss that would have arisen if an exposure goes into default and the only source for collecting the receivable is the realization of the collateral. The loss is measured as a percentage of Exposure at Default (EAD).

The Group has determined relative thresholds that are used also for the exposures for which the absolute thresholds are applied and for those, for which no such thresholds have been determined. They are based on matrixes covering the overall credit cycle (through-the-cycle, TTC) and the change in the probability of default on the respective exposures from the external aggregated data of Moody's (the Group has developed preliminary a methodology for equalizing the internal credit ratings to those assigned by the rating agency).

Expected credit losses on portfolio guarantees issued

These costs/losses are determined on the basis of the present value of the future net cash flows, representing the difference between the payment obligation and the possible inflows of subsequent recourse to third parties.

These costs/losses are determined on the basis of the present value of the future net cash flows, representing the difference between the payment obligation and the possible inflows of subsequent recourse to third parties.

In order to properly assess the portfolios under guarantee schemes in terms of own risk, namely "Guarantee scheme 2009-2011", "Guarantee scheme 2015-2017", "Guarantee scheme 2017-2018" and COSME Guarantee scheme, the NGF applies a Policy on the Classification and Evaluation of Instruments covered by IFRS 9, a Credit Portfolios Rating Procedure and the Methodology for determining the expected credit losses, as also a Procedure for their calculation. A calculation of expected losses on financial instruments in the NGF portfolio

is carried out by applying a calculation model for expected losses. The model for determining expected credit losses is based on the following principles:

- carrying out an impartial evaluation through probability weighting of a set of possible outcomes;
- reflecting the time value of money;
- using relevant and supporting information on past and current events, as well as forecasts of future ones, which is available at the reporting date without incurring excessive costs or making excessive efforts;
- using a current credit risk assessment of counterparties;
- reflecting an estimate of a set of macro-economic data.

In compliance with the requirements of IFRS 9, financial instruments are allocated in three phases – Phase 1, Phase 2 and Phase 3. The allocation is made on the basis of an evaluation of the changes in the counterparties' credit quality compared to their initial approval. The principle rules for allocating the exposures in phases are as follows:

1. A quantitative factor – if the Fund has made a payment on an off-balance sheet asset and the latter has been converted into a balance-sheet asset, the exposure is classified in Phase 3; an asset may be classified as non-performing if the financing bank has provided information that the asset / counterparty has been classified as non-performing or upon an examination carried out by the Fund, which has established an increased risk of occurrence of an event of non-performance.
2. Qualitative factors:
 - 2.1 An absolute threshold – passing below a specific assigned internal rating or an accepted external rating is considered to be a basis for classification under Phase 2 or Phase 3;
 - 2.2 Relative threshold – if a significant deterioration in the counterparty's credit quality compared to the level at initial approval of the exposure above a defined relative threshold is considered, it should be considered as grounds for classification under Phase 2 or Phase 3;

The probability of default is calculated by regression of the residual systemic risk variable, which is assessed on the basis of forecast macro-economic information, by completing the following steps:

1. Calculation of the residual systemic risk variable for each year on the basis of global level data of default by years (according to a simplified Merton formulae, which takes into account an entity's performance as a function of two factors – the entity's idiosyncratic risk and residual systemic risk; the model reports a constant sensitivity ratio of the two factors for all ratings).
2. A regression analysis of the residual systemic risk variable is carried out against different macroeconomic variables; as a result of the analysis, the two best macro-economic variables are selected (which explain the model to the highest extent and are not correlated).
3. Calculation of estimated residual variables for systemic risk based on the selected macroeconomic indicators and calculated regression factors.
4. Calculation of the current estimate of the probability of default within a short period of time based on the estimated residual variables for systemic risk.

Main groups of assets subject to impairment

The following tables present the movements in the main groups of assets subject to impairment between the different phases for the period 01 January – 31 December 2018

Assets measured at amortised cost (except for General Government and Receivables from Banks)	Phase 1	Phase 2	Phase 3	Total
Balance as of 01.01.2018	469,868	129,631	264,924	864,424
Transfers:				
Transfer from Phase 1 to Phase 2	(36,925)	36,925		-
Transfer from Phase 1 to Phase 3	(3,645)		3,645	-
Transfer from Phase 2 to Phase 3		(8,037)	8,037	-
Transfer from Phase 2 to Phase 1	1,233	(1,233)		-
New or acquired exposures	113,830	31,021	14,631	159,483
Repaid or transferred	(114,142)	(21,355)	(103,711)	(239,208)
Increased exposure on existing loans or clients	241,087	108,931	82,786	432,804
Balance as of 31.12.2018	671,307	275,883	270,313	1,217,503

All assets measured at amortised cost – non-financial entities, including with state participation, individuals and non-banking financial institutions are included in the above table.

Assets measured at amortised cost - General Government	Phase 1	Phase 2	Phase 3	Total
Balance as of 01.01.2018	737,516	-	-	737,516
New or acquired exposures	8,179	-	-	8,179
Repaid or transferred	(549,510)	-	-	(549,510)
Increased exposure on existing loans or clients	276,618	-	-	276,618
Balance as of 31.12.2018	472,803	-	-	472,803

The Bank presents under the heading of General Government assets measured at amortised cost relating mainly to the Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP). The loans for Military Medical Academy (MMA), acquired through a cession contract, were paid fully in 2018.

Assets measured at amortised cost - Banks and financial institutions	Phase 1	Phase 2	Phase 3	Total
Balance as of 01.01.2018	198,683	-	-	198,683
New or acquired exposures	343,246	-	-	343,246
Repaid or transferred	(113,513)	-	-	(113,513)
Increased exposure on existing loans or clients	2,707	-	-	2,707
Balance as of 31.12.2018	431,122	-	-	431,122

Loans to banks and financial institutions include both transactions on an interbank market and deposits of different maturity.

Assets measured at fair value through other comprehensive income	Phase 1	Phase 2	Phase 3	Total
Balance as of 01.01.2018	292,461	-	-	292,461
New or acquired exposures	315,141	-	-	315,141
Repaid or transferred	(81,571)	-	-	(81,571)
Increased exposure on existing loans or clients	127,626	-	-	127,626
Balance as of 31.12.2018	653,657	-	-	653,657

Portfolio of securities consists mainly of bonds of the Republic of Bulgaria, other European sovereign issuers and bonds of large corporate clients.

Movement in the impairment of main groups of assets subject to impairment in 2018

The amount of the expected credit loss is a function of the probability of default of the instrument, the realized loss and the amount of balance sheet and off-balance sheet exposure. The probability of default (PD) and the realized LGD are the parameters employed in determining the provisioning rate and those parameters are determined on the basis of an individual review of the early warning signs that are homogeneous in terms of their credit characteristics and their relation to international and domestic macroeconomic variables that could affect them.

Movement in impairment in 2018:

Assets measured at amortised cost (except for General Government)	Phase 1	Phase 2	Phase 3	Total
Balance of impairment as of 01.01.2018	4,020	902	156,127	161,049
Transfers:				
Transfer from Phase 1 to Phase 2	(915)	915		-
Transfer from Phase 1 to Phase 3	(417)		417	-
Transfer from Phase 2 to Phase 3		(2,048)	2,048	-
Transfer from Phase 2 to Phase 1	2	(2)		-
New or acquired exposures	2,561	185	-	2,746
Repaid or transferred	(4,074)	(902)	(60,340)	(65,316)
Increased exposure on existing loans or clients	3,610	3,106	54,732	61,448
Balance of impairment as of 31.12.2018	4,787	2,156	152,984	159,927

Assets measured at amortised cost - General Government	Phase 1	Phase 2	Phase 3	Total
Balance of impairment as of 01.01.2018	1,432	-	-	1,432
Net movement in impairment on Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP)	(824)	-	-	(824)
Repayment of cessions Military Medical Academy (MMA)	196	-	-	196
Balance of impairment as of 31.12.2018	804	-	-	804

Assets measured at fair value through other comprehensive income	Phase 1	Phase 2	Phase 3	Total
Balance of impairment as of 01.01.2018	708	-	-	708
New exposures	7,249	-	-	7,249
Repaid or transferred	(4,926)	-	-	(4,926)
Other movements	(628)	-	-	(628)
Balance of impairment as of 31.12.2018	2,403	-	-	2,403

Amount of the collateral as of 31.12.2018

The amount of the collateral on secured assets is presented in the following table:

Type of collateral	Carrying amount of the loan, BGN'000*	Amount of the collateral, BGN'000
Mortgages	569,590	514,012
Pledge of plant, equipment and inventories	375,483	148,321
Restricted deposits	200,600	273,290
Mortgage on a ship	58,102	4,164
Insurances	27,343	18,482
Bank guarantees	22,631	3,863
Securities	14,718	20,536
Total	1,268,467	982,668

**These amounts do not include the balance on the portfolio of MFI JOBS for the total carrying amount of BGN 14,384 thousand.*

Country (sovereign) risk

The Group has formed a portfolio of securities classified as financial assets at fair value through other comprehensive income, comprising only government securities issued by the Republic of Bulgaria. The Group's exposure to sovereign was BGN 599,567 thousand as of 31 December 2018 and BGN 288,881 thousand as of 31 December 2017.

Standard & Poor's credit rating for Republic of Bulgaria stands at BBB – with stable outlook (1 December 2017). Fitch's credit rating for Republic of Bulgaria is BBB with stable outlook (23 March 2019). Moody's credit rating for Republic of Bulgaria was last set at Baa2 with stable outlook (26 May 2017).

According to Fitch Ratings, BBB credit rating means that insolvency expectations are low, and the capacity to service financial liabilities is adequate, but a deterioration in economic conditions or business environment is likely to lessen this capacity. The definitions of Moody's and Standard Poor's of the rating assigned to the sovereign are similar.

4.2. Market risk

Market risk is the risk of adverse movements in interest rates, exchange rates, liquidity position, and other factors affecting the price of securities and other financial assets. These movements affect the Group's profitability and financial position.

Interest rate risk

Interest rate risk is the probability for potential change of the net interest income or the net interest margin and the market value of the equity due to changes in market interest rates.

Interest rate risk is considered in view of the overall activity of the Group. Analyses of financial assets and liabilities grouped in time intervals depending on their sensitivity to changes in the interest rates are conducted on regular basis.

The approach for measuring interest rate risk with respect to the overall activity comprises primarily:

- Analysis of the interest rate sensitivity of income – measuring the interest rate sensitivity of the Group's net income;
- Analysis of the interest rate sensitivity of economic capital (Duration GAP Analysis) – measuring the interest rate sensitivity of the Group's economic value;
- Determination, application and reporting of limits for interest rate risk reflecting the volatility of the respective interest rate curve and the Group's risk appetite;
- Stress tests for interest rate risk – presenting the potential movements in the annual interest income after applying a stress scenario involving changes in the interest rate curves by types of currencies.

Cash flow interest rate analysis is conducted by allocating the cash flows from assets and liabilities included in the interest rate imbalance analysis and forming the respective maturity gaps. In case of Group's balance sheet items classified as such and measured at fair value, the fair value risk analysis is limited to placing the relevant item with the applicable maturity structure within the interest rate imbalance analysis.

In addition to interest rate sensitivity analyses, the main drivers of the movement in the net interest spread of the Group are identified for the purposes of interest rate risk management. This assists decision making on the interest rate policies of the Group, in particular, for the development of specific products and providing sources of financing having matching characteristics.

The Assets and Liabilities Committee (ALCO) currently monitors interest rate risk to which the Group is exposed and develops measures for its management and maintenance within the Group's permitted levels and limits.

The tables on this and on the next page summarise the interest exposure and interest risk of the Group. It includes information on the Group's assets and liabilities at their carrying amount in accordance with interest-related clauses, set in the contracts, their maturity structure and sensitivity to movements in interest rates.

31 December 2018	<i>With floating interest rate %</i>	<i>With fixed interest rate %</i>	<i>Interest- free</i>	<i>Total</i>
Financial assets				
Receivables from banks	4,961	414,499	10,543	429,978
Loans and advances to customers	1,004,854	41,980	1,200	1,048,034
Receivables from the State budget	471,999	-	-	471,999
Financial assets at fair value through other comprehensive income	-	650,374	3,283	653,657
Net investment in finance lease	932	-	-	932
Securities at amortised cost	-	10,216	-	10,216
Other financial assets	-	-	908	908
	1,482,746	1,117,069	15,934	2,615,724
Financial liabilities				
Deposits from credit institutions	5,759	-	-	5,759
Deposits from customers other than credit institutions	679,801	465,323	26,701	1,171,825
Borrowings from international institutions	727,017	177,765	-	904,782
Other borrowings	11,236	6,070	93,025	110,331
	1,423,813	649,158	119,726	2,192,697
Total interest rate exposure	58,933	467,911	(103,792)	423,027
Contingencies and commitments	328,077	20,300	465,491	813,868

31 December 2017	<i>With floating interest rate %</i>	<i>With fixed interest rate %</i>	<i>Interest- free</i>	<i>Total</i>
Financial assets				
Receivables from banks	6,196	182,172	10,542	198,910
Loans and advances to customers	658,611	50,500	-	709,111
Receivables from the State budget	728,010	9,506	-	737,516
Available-for-sale securities	-	288,881	2,986	291,867
Net investment in finance lease	1,035	-	-	1,035
Securities held to maturity	594	-	-	594
Other financial assets	-	-	727	727
	1,394,446	531,059	14,255	1,939,760
Financial liabilities				
Deposits from credit institutions	3,897	30,012	-	33,909
Deposits from customers other than credit institutions	577,760	59,913	22,174	659,847
Borrowings from international institutions	663,490	206,332	-	869,822
Other borrowings	11,236	6,256	93,914	111,406
	1,256,383	302,513	116,088	1,674,984
Total interest rate exposure	138,063	228,546	(101,833)	264,776
Contingencies and commitments	442,641	3,582	409,349	855,572



Analysis of interest rate sensitivity and risk

The table below includes the financial instruments of the Group, presented at carrying value, classified by the earlier of the date of interest rate change under the contract and the maturity date.

31 December 2018	Within 1 month	1-3 months	3-6 months	6-12 months	1-5 years	Over 5 years	With fixed interest rate	Interest-free	Total
Financial assets									
Receivables from banks	4,961	-	-	-	-	-	414,499	10,543	430,003
Loans and advances to customers	78,338	926,703	76	94	89	-	414,499	1,200	1,048,034
Receivables from the State budget	471,999	-	-	-	-	-	41,534	-	471,999
Financial assets at fair value through other comprehensive income	76,821	8,635	-	8,961	298,027	257,930	-	3,283	653,657
Net investment in finance leases	932	-	-	-	-	-	-	-	932
Securities at amortised cost	-	-	-	-	-	10,216	-	-	10,216
Other financial assets	-	-	-	-	-	-	-	908	908
Total financial assets	633,051	935,338	76	9,055	298,116	268,146	456,033	15,934	2,615,749
Financial liabilities									
Deposits from credit institutions	5,759	-	-	-	-	-	-	-	5,759
Deposits from customers other than credit institutions	758,783	3,710	378,083	2,694	1,854	-	-	26,701	1,171,825
Borrowings from international institutions	101,397	251,770	373,850	-	-	-	177,765	-	904,782
Other borrowings	-	11,236	-	-	93,025	6,070	-	-	110,331
						6,070	177,765		
Total financial liabilities	865,939	266,716	751,933	2,694	94,879		177,765	26,701	2,192,697
Total exposure to interest rate sensitivity	(232,888)	668,622	(751,857)	6,361	203,237	262,076	278,268	(10,767)	423,027
Contingencies and commitments	54,295	43,477	7,789	79,578	142,938	-	20,300	465,491	813,868



31 December 2017	Within 1 month	1-3 months	3-6 months	6-12 months	1-5 years	With fixed interest rate	Interest-free	Total
Financial assets								
Receivables from banks	2,713	3,483	-	-	-	182,172	10,542	198,910
Loans and advances to customers	89,475	567,333	103	220	1,480	50,500	-	709,111
Receivables from the State budget	728,010	-	-	-	-	9,506	-	737,516
Available-for-sale securities	67,346	-	-	-	151,728	69,807	2,986	291,867
Net investment in finance leases	1,035	-	-	-	-	-	-	1,035
Securities held to maturity	594	-	-	-	-	-	-	594
Other financial assets	-	-	-	-	-	-	727	727
Total financial assets	889,173	570,816	103	220	153,208	311,985	14,255	1,939,760
Financial liabilities								
Deposits from credit institutions	3,897	30,012	-	-	-	-	-	33,909
Deposits from customers other than credit institutions	508,119	1,406	436	16,330	111,382	-	22,174	659,847
Borrowings from international institutions	1,838	23,255	4,053	48,519	293,848	498,309	-	869,822
Other borrowings	-	11,236	-	-	-	6,256	93,914	111,406
Total financial liabilities	513,854	65,909	4,489	64,849	405,230	504,565	116,088	1,674,984
Total exposure to interest rate sensitivity	375,319	504,907	(4,386)	(64,629)	(252,022)	(192,580)	(101,833)	264,776
Contingencies and commitments	1,355	12	9,274	31,413	404,169	-	409,349	855,572

Sensitivity of the floating rate interest assets and liabilities

The table below represents the sensitivity of the Group to possible changes in interest rates based on the structure of floating rate assets and liabilities as of 31 December, under the assumption that the influence of the other variables is ignored. The actual effect of changes in market interest rates could be different, as a significant portion of the loans and receivables from customers bear floating interest rates that are based on a variable portion determined by the Group, which in turn is influenced by numerous factors.

Currency	2018			2017		
	Increase %	Sensitivity of the financial result	Sensitivity of the equity	Increase %	Sensitivity of the financial result	Sensitivity of the equity
BGN	0.50%	819	(3,617)	0.50%	1,981	(2,221)
EUR	0.50%	(454)	(9,160)	0.50%	(1,291)	(1,627)
USD	0.50%	(237)	(32)	0.50%	(153)	-
BGN	-0.50%	(819)	3,617	-0.50%	(1,981)	2,221
EUR	-0.50%	454	9,160	-0.50%	1,291	1,627
USD	-0.50%	237	32	-0.50%	153	-

The average interest rates by financial assets and financial liabilities are presented in the following table:

	31.12.2018	31.12.2017
Financial assets	2,66%	2,35%
Financial liabilities	0,37%	0,43%

Currency risk

The currency risk is the risk that the financial position and cash flows of the Group might be affected adversely by changes in exchange rates due to open currency positions. In managing the foreign currency risk, the Group follows the principle of maintaining minimum open currency positions within the specified limits. Foreign currency positions are not formed with speculative purposes, but arise out of foreign currency transactions in the ordinary course of business of the Group.

The policy of the parent company (the Bank) is that the main portion of the assets and liabilities, and respectively the bank transactions, shall be denominated in EUR or BGN. The Group does not carry out significant transactions and does not hold significant open positions in currencies other than EUR and BGN. As the exchange rate of the Bulgarian lev is pegged to that of the Euro, there is no significant open currency risk for the Group's cash flows and financial performance.

The following table summarises the Group's exposure to currency risk. The table includes the Group's financial instruments and the contingent liabilities and commitments, presented at carrying amount, classified by type of currency.

At 31 December 2018	In USD	In EUR	In other foreign currency	In BGN	Total
Financial assets					
Cash in hand and balances in current account with the Central Bank	28	4,178	-	293,416	297,622
Receivables from banks	114,399	122,449	57	193,098	430,003
Loans and advances to customers	-	734,374	-	313,660	1,048,034
Receivables from the State budget	-	-	-	471,999	471,999
Financial assets at fair value through other comprehensive income	17,597	463,954	-	172,106	653,657
Net investment in finance leases	-	-	-	932	932
Securities at amortised cost	-	10,216	-	-	10,216
Other financial assets	-	-	-	908	908
Total financial assets	132,024	1,335,171	57	1,446,119	2,913,371
Financial liabilities					
Deposits from credit institutions	-	1,465	-	4,294	5,759
Deposits from customers other than credit institutions	131,979	96,648	40	943,158	1,171,825
Borrowings from international institutions	-	904,782	-	-	904,782
Other borrowings	-	17,306	-	93,025	110,331
Total financial liabilities	131,979	1,020,201	40	1,040,477	2,192,697
Net balance sheet currency position	45	314,969	17	405,618	720,649
Contingencies and commitments	1,025	206,657	-	606,186	813,868

As at 31 December 2017	In USD	In EUR	In other foreign currency	In BGN	Total
Financial assets					
Cash in hand and balances in current account with the Central Bank	30	4,748	-	442,870	447,648
Receivables from banks	76,461	23,864	144	98,441	198,910
Loans and advances to customers	-	479,156	1,009	228,946	709,111
Receivables from the State budget	-	-	-	737,516	737,516
Available-for-sale securities	-	111,382	-	180,485	291,867
Net investment in finance leases	-	-	-	1,035	1,035
Securities held to maturity	-	594	-	-	594
Other financial assets	-	-	-	727	727
Total financial assets	76,491	619,744	1,153	1,690,020	2,387,408
Financial liabilities					
Deposits from credit institutions	-	2,013	-	31,896	33,909
Deposits from customers other than credit institutions	76,484	69,886	92	513,385	659,847
Borrowings from international institutions	-	868,802	1,020	-	869,822
Other borrowings	-	17,492	-	93,914	111,406
Total financial liabilities	76,484	958,193	1,112	639,195	1,674,984
Net balance sheet currency position	7	(338,449)	41	1,050,825	712,424
Contingencies and commitments	408	59,176	-	795,988	855,572

The following table presents the Group's sensitivity to possible changes in exchange rates based on the structure of the assets and liabilities at 31 December:

2018						
Currency	Change in exchange rates			Effect on the pre-tax profit in case of change in exchange rates*		Effect on equity
	Exchange rate	Decrease (BPS)	Increase (BPS)	Decrease	Increase	
EUR	1.9558	-	-	-	-	-
USD	1.7082	1,201	-1,337	-28	31	-
JPY	0.0155	17	-16	0	0	-
GBP	2.1864	-2,504	1,005	-2	1	-
Total effect				-30	32	-

2017						
Currency	Change in exchange rates			Effect on the pre-tax profit in case of change in exchange rates*		Effect on equity
	Exchange rate	Decrease (BPS)	Increase (BPS)	Decrease	Increase	
EUR	1.9558	-	-	-	-	-
USD	1,6308	-1,270	+2,068	31	(51)	-
JPY	0,0145	-15	+18	(3)	4	-
GBP	2,2044	-2,524	+1,987	(3)	2	-
Total effect				25	(44)	-

The open FX position and the market volatility of the respective foreign currencies as at 31 December 2018 would have an immaterial effect on the Group's financial result assessed as equal to minus BGN 30 thousand if the hypothesis of unfavourable change in exchange rates occurs compared to the open positions of the Bank by separate currencies with the reported basis points (BPS: 1 b.p. = 0.0001 in decimal form).

Price risk of shares quoted on a securities exchange

The Group is exposed to price risk with respect to the shares it holds, classified as investments at fair value through other comprehensive income. Management of the parent company (the Bank) monitors and analyses all changes in the security market, and engages the advisory services of renowned local investment intermediaries. In addition, at this stage management of the parent company (the Bank) has decided to greatly reduce the operations on the stock markets and the trade in the acquired shares, and currently monitors the financial and business indicators, reported by the respective issuer, as well as the development of its activities.

4.3. Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its current and potential payment obligations as they fall due without suffering losses.

The Group's business requires a stable cash flow both to replace existing deposits and loans received prior to their maturity, and to satisfy demands of customers for additional loans. Undrawn borrowing facility commitments and the level of all outstanding contingent obligations are taken into consideration in managing the parent company's (the Bank's) liquidity risk.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, as well as the impact of the changes in interest rates and exchange rates on the pre-tax profit and equity, are important factors in assessing the Group's liquidity. In order to manage this risk, the Group maintains at all times highly liquid assets depending on the currency of its liabilities.

The overall liquidity control and monitoring are performed by ALCO and are based on maturity tables with scenarios for measuring the net cash flows by periods, including nominal, realistic and pessimistic scenario, reflecting to a different degree the negative assumptions relating to loss of confidence by the customers, deterioration of the credit portfolio quality, negative assumptions about the banking market and other assumptions having an impact on the Group's liquid position and certain ratios enacted by Bulgarian National Bank. Additionally, a number of correlations are monitored to indicate the liquid position by periods. Liquidity risk is also measured through application of three additional scenarios for the cash flows from operating activities and monitoring the liquidity buffers of the parent company (the Bank) and the additional sources of financing in case of market and idiosyncratic shocks, representing loss of confidence by the market in a particular bank or banking group, which is tantamount to downgrading of the institution with two degrees at least and combined shocks in compliance with the Guidelines on liquidity buffers and survival periods of Bulgarian National Bank.

The table below presents the amounts in percentage of the liquidity coverage ratio (LCR) of parent company (the Bank)

	2018	2017
As of 31 December	1,331.20%	301.05%
Average for the period	1,053.40%	216.71%
Highest for the period	1,785.50%	457.21%
Lowest for the period	424.26%	91.61%
Cash and cash balances with BNB	297,622	447,648
Balances in current accounts with other banks and international deposits of up to 7 days	319,679	73,968
Government securities	609,783	227,917
Liquid assets	1,227,084	749,533
Financial liabilities measured at amortised cost	2,192,697	1,711,813
Provisions	7,829	930
Employee retirement benefits	400	366
Liabilities	2,200,925	1,713,109
Liquid assets ratio (LAR)	1,331.20%	43.75%



The table below provides an analysis of the financial assets and liabilities of the Group grouped by remaining maturity (assets with indefinite maturity have a long-term period of realisation):

At 31 December 2018	Within 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite maturity	Total
Assets							
Cash in hand and balances in current account with the Central Bank	297,622	-	-	-	-	-	297,622
Receivables from banks	219,082	102,757	10,317	1,644	96,203	-	430,003
Loans and advances to customers	52,376	36,929	145,677	447,240	365,812	-	1,048,034
Receivables from the State budget	23,756	143,647	304,596	-	-	-	471,999
Financial assets at fair value through other comprehensive income	78,151	10,849	11,606	240,177	309,591	3,283	653,657
Net investment in finance lease	19	36	177	671	29	-	932
Assets held for sale	-	-	5,012	-	-	-	5,012
Current tax liabilities	-	-	1,774	-	-	-	1,774
Securities held to maturity	-	-	-	-	10,216	-	10,216
Other assets	-	-	1,609	-	-	-	1,609
Assets acquired from collateral foreclosure	-	-	-	27,128	-	-	27,128
Investment property	-	-	-	-	-	7,649	7,649
Property, plant and equipment, intangible assets	-	-	-	-	-	37,597	37,597
Deferred tax assets	-	-	261	-	-	-	261
Total assets	671,006	294,218	481,029	716,860	781,851	48,529	2,993,493
Liabilities							
Deposits from credit institutions	5,759	-	-	-	-	-	5,759
Current tax liabilities	-	-	22	-	-	-	22
Deposits from customers other than credit institutions	760,080	3,966	393,462	13,296	1,021	-	1,171,825
Provisions	-	-	-	-	-	7,828	7,828
Other liabilities	1,626	-	-	118	-	1,036	2,780
Borrowings from international institutions	1,837	21,992	597,177	-	283,776	-	904,782
Other borrowings	-	-	213	93,985	16,133	-	110,331
Total liabilities	769,302	25,958	990,874	107,999	300,930	8,864	2,203,327
Gap in maturity thresholds of assets and liabilities	(98,296)	268,260	(509,845)	609,461	480,921	39,665	790,166
Contingencies and commitments	58,248	51,252	97,015	157,552	23,256	408,059	795,382



As at 31 December 2017	Within 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite maturity	Total
Assets							
Cash in hand and balances in current account with the Central Bank	447,648	-	-	-	-	-	447,648
Receivables from banks	75,817	122	19,377	10,947	92,647	-	198,910
Loans and advances to customers	23,699	13,141	131,990	321,877	218,404	-	709,111
Receivables from the State budget	-	-	-	737,516	-	-	737,516
Available-for-sale securities	67,346	-	-	137,562	83,973	2,986	291,867
Net investment in finance lease	17	39	174	767	38	-	1,035
Assets held for sale	-	-	10,100	-	-	-	10,100
Current tax receivables	-	-	1,596	-	-	-	1,596
Securities held to maturity	7	-	587	-	-	-	594
Other assets	-	-	1,390	-	-	-	1,390
Assets acquired from collateral foreclosure	-	-	-	15,875	-	-	15,875
Investment property	-	-	-	-	-	7,702	7,702
Property, plant and equipment, intangible assets	-	-	-	-	-	32,999	32,999
Deferred tax assets	-	-	2,258	-	-	-	2,258
Total assets	614,534	13,302	167,472	1,224,544	395,062	43,687	2,458,601
As at 31 December 2017							
Liabilities							
Deposits from credit institutions	3,897	30,012	-	-	-	-	33,909
Current tax liabilities	-	98	-	-	-	-	98
Deposits from customers other than credit institutions	635,529	1,044	9,873	13,401	-	-	659,847
Provisions	-	-	-	-	-	5,856	5,856
Other liabilities	1,902	-	-	510	-	427	2,839
Borrowings from international institutions	1,838	23,255	94,613	458,138	291,978	-	869,822



As at 31 December 2017	Within 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Indefinite maturity	Total
Other borrowings	-	-	213	94,767	16,426	-	111,406
Total liabilities	643,166	54,409	104,699	566,816	308,404	6,283	1,683,777
Gap in maturity thresholds of assets and liabilities	(28,632)	(41,107)	62,773	657,728	86,658	37,404	774,824
Contingencies and commitments	6,304	1,891	64,026	439,610	-	333,134	844,965

The table below presents the gross undiscounted cash flows related to the Group's liabilities as of 31 December:

As at 31 December 2018	Carrying amount	Gross flow	Less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years
Financial liabilities							
Deposits from credit institutions	5,759	5,759	5,759	-	-	-	-
Deposits from customers other than credit institutions	1,171,825	1,171,904	760,082	3,967	393,528	13,305	1,022
Borrowings from international institutions	904,782	954,593	1,837	22,086	611,195	-	319,475
Other borrowings	110,331	111,934	-	30	303	94,498	17,103
	2,192,697	2,244,190	767,678	26,083	1,005,026	107,803	337,600
Bank guarantee provisions	4,701	4,701	300	600	3,801	-	-
Unutilised credit commitments	328,324	328,324	54,295	43,477	67,314	142,938	20,300

As at 31 December 2017	Carrying amount	Gross flow	Less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years
Financial liabilities							
Deposits from credit institutions	33,909	33,912	3,897	30,015	-	-	-
Deposits from customers other than credit institutions	659,847	660,765	635,530	1,045	9,932	14,258	-
Borrowings from international institutions	869,822	905,278	1,838	23,379	95,187	465,399	319,475
Other borrowings	111,406	113,116	-	31	306	95,221	17,558
	1,674,984	1,713,071	641,265	54,470	105,425	574,878	337,033
Bank guarantee provisions	5,829	5,829	600	1,133	3,000	1,096	-
Unutilised credit commitments	446,223	446,223	1,364	13	42,450	402,396	-

Considering the specific activity of the Group, the funds attracted from the biggest 20 non-bank depositors at 31 December 2017 represent 97.13 per cent of the total amount of payables to other customers (31 December 2016: 97.10 per cent). The share of the biggest non-bank depositor of the total amount of payables to other customers is 46.07 per cent (31 December 2016: 56.91 per cent).

The financial assets available for future financing and the financial assets pledged as collateral for financial liabilities are presented in the table below:

At 31 December 2018				
Financial assets	Pledged as collateral	Available for collateral	Other* ¹	Total
Cash in hand and balances in current account with the Central Bank	-	125,479	172,143	297,622
Receivables from banks	10,543	419,460	-	429,978
Net investments in finance leases	-	932	-	932
Loans and advances to customers	-	665,559	382,475	1,048,034
Receivables from the State budget	-	471,999	-	471,999
Financial assets at fair value through other comprehensive income	6,633	644,302	2,722	653,657
Securities at amortised cost	-	10,216	-	10,216
Other financial assets	-	-	908	908
Total financial assets	17,176	2,337,947	558,248	2,913,371

At 31 December 2017				
Financial assets	Pledged as collateral	Available for collateral	Other*	Total
Cash in hand and balances in current account with the Central Bank	-	327,248	120,400	447,648
Receivables from banks	10,542	187,837	-	198,379
Loans and advances to customers	-	526,965	172,715	699,680
Receivables from the State budget	-	737,516	-	737,516
Available-for-sale securities	7,515	220,768	2,620	230,903
Securities held to maturity	-	594	-	594
Other financial assets	-	-	36	36
Total financial assets	18,057	2,000,928	295,771	2,314,756

* At 31 December 2018, funds amounting to BGN 10,543 thousand (2017: BGN 10,542 thousand) were blocked in counter-guarantees of two corporate customers, maturing as follows:

Maturity interval	Receivables from banks pledged as collateral
On demand	182
From 91 to 180 days	2,712
From 181 to one year	6,479
Over one year	1,170

At 31 December 2018, securities on a legal requirement to provide for funds of the State budget amounting to BGN 7,256 thousand (2017: BGN 7,515 thousand) were blocked.

Review of the size, development and the credit quality of the unencumbered assets is done once a year.

Risk Management, together with other Group divisions, monthly monitors and reports to ALCO on the ratios between the encumbered assets and the total carrying amount of the Group's assets. In a case of excess above the limits approved by the Management Board, ALCO reports back to the MB for undertaking corrective actions.

4.4. Operational risk

The main sources of operational risk within the Group are its personnel, processes, systems and external events. The Group designated the following as the major types of operational risk:

- Risk of loss due to inadequate or poorly working internal processes;
- Risk of loss due to inadequate, illegal and/or incorrect acts and omissions of personnel;
- Risk of loss due to inadequate or poorly working systems;
- Risk of loss due to external events, including legal risk.

Operational risk management is based on the principles of not taking unreasonable risks, strict compliance with the levels of competence and the applicable legislation. The Group applies reliable methods for limiting the impact of operational risks, including by dividing the functions and responsibilities, introducing double-checking control, levels of competence, internal control, etc. Moreover, control procedures for reducing the operational risk are added to all internal rules and procedures of the Group.

In operational risk management all operational events, which occur in the activity of various units and processes of the Group, are strictly monitored and registered, while the events of higher frequency, as well as those of significant importance, serve as bases for the operational risk analyses in different scenarios. The operational risk is measurable and monitorable, and in the process of work an operational event register is kept, which is used as a basis for analysing and improving the work processes, and minimising the conditions that would potentially result in operational events and loss for the Group. For the purposes of measuring its operational risk, the Group has decided to apply the "Basic indicator method".

4.5. Equity management

The main objectives of the Group's capital management is to maintain its level at amounts sufficient for activity developing and achieving the general objectives set at its foundation – to support the economic policy of the country and the development of small and medium-sized businesses.

In its activities the Group should observe the regulatory requirements for capital adequacy (Notes 33, 34), as well as to continue operating as a going concern.

The table below presents the main equity components following the regulatory requirements and ratios achieved on a consolidated group (as a Bank group) level.

	2018	2017
OWN FUNDS	746,915	739,513
TIER I CAPITAL	746,915	739,513
COMMON EQUITY TIER I CAPITAL	746,915	739,513
Share capital	601,774	601,774
Statutory reserves	73,672	71,989
Additional reserves	76,190	68,105
Accumulated other comprehensive income	10,901	10,961
Intangible assets	(331)	(282)
Investments in subsidiaries	(20,482)	-
Other transitional adjustments to CET1 Capital	(9,649)	(2,620)
Components of or deductions from CET 1 Capital – other	(4,458)	(10,829)
ADDITIONAL TIER I CAPITAL	-	-
TIER II CAPITAL	-	-
TOTAL RISK EXPOSURES	2,071,469	1,495,506
Credit risk – Standardised approach	1,891,995	1,380,418
Central governments or central banks	52,367	-
Regional governments or local authorities	-	202
Public sector entities	-	9,506
Multilateral development banks	939	939
Institutions	184,895	125,719
Corporates	1,123,264	852,895
Retail	12,270	17,325
Secured by mortgages on immovable property	265,587	101,621
Exposures in default	170,642	191,704
Items associated with particular high risk	2,934	2,936
Equity exposures	199	152
Other items	78,898	77,419
Currency risk	59,461	-
Operational risk – Basic indicator approach	120,013	115,088
CET 1 Capital Ratio	36.06%	49.45%
Total Capital Ratio	36.06%	49.45%

	2018	2017
Capital conservation buffer	51,787	37,388
Systemic risk buffer	62,144	44,863
Discretionary counter-cyclical buffer	-	-
Buffer of other institutions of systemic importance	2,589	-
Regulatory required levels		
CET 1 Capital Ratio	4.50%	4.50%
Tier 1 Capital ratio	6.00%	6.00%
Total Capital ratio	8.00%	8.00%
Capital conservation buffer	2.50%	2.50%
Systemic risk buffer	3.00%	3.00%
Discretionary counter-cyclical buffer	-	-
Buffer of other institutions of systemic importance	0.125%	-



5. FAIR VALUE DISCLOSURE

The table below presents the carrying amount and fair values of financial assets and liabilities, including by their levels in the fair value hierarchy:

		Carrying amount						Fair value				
		Note	Held-to-maturity	Loans and receivables	Held-for-trading	other comprehensive income	Other	Total	Level 1	Level 2	Level 3	Total
At 31 December 2018												
Assets at fair value												
Financial assets at fair value through other comprehensive income	21	-	-	-	-	653,657	-	653,657	652,928	-	-	652,928
Assets acquired from collateral foreclosure	26	-	-	-	-	-	27,128	27,128	-	-	27,128	27,128
Investment property	25	-	-	-	-	-	7,649	7,649	-	-	7,649	7,649
		-	-	-	-	653,657	34,777	688,434	652,928	-	34,777	687,705
Financial assets not measured at fair value												
Cash in hand and balances in current account with the Central Bank	16	-	297,622	-	-	-	-	297,622	-	297,622	-	297,622
Loans to banks	17	-	99,297	-	-	-	-	99,297	-	104,943	-	104,943
Current accounts and term deposits of banks	17	-	330,681	-	-	-	-	330,681	-	330,681	-	330,681
Loans and advances to customers	18	-	1,048,034	-	-	-	-	1,048,034	-	1,078,909	-	1,078,909
Receivables from the State budget	19	-	471,999	-	-	-	-	471,999	-	497,667	-	497,667
Securities held to maturity	20	10,216	-	-	-	-	-	10,216	-	13,055	-	13,055
		10,216	2,247,633	-	-	-	-	2,257,849	-	2,322,877	-	2,322,877
Financial liabilities not measured at fair value												
Deposits from credit institutions – Current accounts and term deposits of banks	28	-	-	-	-	-	5,759	5,759	-	5,759	-	5,759
Deposits from customers other than credit institutions	29	-	-	-	-	-	1,171,825	1,171,825	-	1,172,236	-	1,172,236
Borrowings from international institutions	30	-	-	-	-	-	904,782	904,782	-	936,612	-	936,612
Other borrowings	31	-	-	-	-	-	110,331	110,331	-	110,894	-	110,894
		-	-	-	-	-	2,192,697	2,192,697	-	2,225,501	-	2,225,501



The fair value of securities classified as investments with carrying amount of BGN 729 thousand at 31 December 2018 (2017: BGN 491 thousand) carried at cost has not been disclosed as the Banks deems it cannot be measured reliably.

At 31 December 2017		Carrying amount					Fair value				
	Note	Held-to-maturity	Loans and receivables	Held-for-trading	Available-for-sale	Other	Total	Level 1	Level 2	Level 3	Total
Assets at fair value											
Available-for-sale securities	21	-	-	-	291,867	-	291,867	291,867	-	-	291,867
Assets acquired from collateral foreclosure	26	-	-	-	-	15,875	15,875	-	-	15,875	15,875
Investment property	25	-	-	-	-	7,702	7,702	-	-	7,702	7,702
		-	-	-	291,867	23,577	315,444	291,867	-	23,577	315,444
Financial assets not measured at fair value											
Cash in hand and balances in current account with the Central Bank	16	-	447,648	-	-	-	447,648	-	447,648	-	447,648
Loans to banks	17	-	113,869	-	-	-	113,869	-	116,576	-	116,576
Current accounts and term deposits of banks	17	-	85,041	-	-	-	85,041	-	85,042	-	85,042
Loans and advances to customers	18	-	709,111	-	-	-	709,111	-	722,807	-	722,807
Receivables from the State budget	19	-	737,516	-	-	-	737,516	-	799,661	-	799,661
Securities held to maturity	20	594	-	-	-	-	594	-	598	-	598
		594	2,093,185	-	-	-	2,093,779	-	2,172,332	-	2,172,332
Financial liabilities not measured at fair value											
Deposits from credit institutions – Current accounts and term deposits of banks	28	-	-	-	-	33,909	33,909	-	33,909	-	33,909
Deposits from customers other than credit institutions	29	-	-	-	-	659,847	659,847	-	659,841	-	659,841
Borrowings from international institutions	30	-	-	-	-	869,822	869,822	-	899,003	-	899,003
Other borrowings	31	-	-	-	-	111,406	111,406	-	112,299	-	112,299
		-	-	-	-	1,674,984	1,674,984	-	1,705,052	-	1,705,052

Fair value of assets and liabilities measured at fair value is presented in the following table by types of assets at the reporting date. The Group discloses voluntary the fair values the assets acquired from collateral foreclosure as of 31 December 2018 and 31 December 2017.



Financial instrument	Fair value as of 31.12.2018	Fair value as of 31.12.2017	Fair value hierarchy	Valuation techniques	Significant unobservable inputs	Relationship of unobservable inputs to fair value
Investment property	7,649	7,702	Level 3	<p>Market analogues method</p> <p>Under the market analogues method an assessment is made by directly comparing the property under review with sold similar properties; the price is determined on the basis of such previous transactions. When applying this approach, it is necessary to use actually similar data of the comparable properties, the properties should be in the same location and the timing of the transaction and the date of preparation of the evaluation should be close enough.</p>	<p>Market realisation coefficient (0.8-0.95)</p> <p>Location coefficient (0.81-1.0)</p> <p>Coefficient of specific features (status) (0.8-.1)</p>	<p>The higher (lower) fair value if: Higher (lower) market realisation coefficient Higher (lower) location coefficient Higher (lower) coefficient of specific features (status)</p>
				<p>Income capitalisation method (revenue method)</p> <p>The revenue method, used for assessing the real estate value, consists of an analysis of the value of the real estate based on its ability to generate income through capitalisation of the net income derived from the property over a given period. For the determination of the evaluated property's amount, the permanently generated net annual income is used and its amount is calculated on the basis of the actual or possible permanently achieved rental income, which it turn is calculated on the basis of the average offered rent in the area (observable inputs), by taking into account the condition of the building fund and the residual term of use.</p>	<p>Offer market adequacy adjustment coefficient (from -10% to +5%)</p>	<p>The higher (lower) fair value if: Higher (lower) offer market adequacy adjustment coefficient</p>



Financial instrument	Fair value as of 31.12.2018	Fair value as of 31.12.2017	Fair value hierarchy	Valuation techniques	Significant unobservable inputs	Relationship of unobservable inputs to fair value
Assets acquired from collateral foreclosure	27,128	15,875	Level 3	Income capitalisation method (revenue method) The revenue method, used for assessing the real estate value, consists of an analysis of the value of the real estate based on its ability to generate income through capitalisation of the net income derived from the property over a given period. For the determination of the evaluated property's amount, the permanently generated net annual income is used and its amount is calculated on the basis of the actual or possible permanently achieved rental income, which it turn is calculated on the basis of the average offered rent in the area (observable inputs), by taking into account the condition of the building fund and the residual term of use.	Offer market adequacy adjustment coefficient (from -10% to +5%)	Higher (lower) correction coefficient for market adequacy of offers.
Loans to banks	104,943	116,576	Level 2	Discounted cash flows Future cash flows are discounted using the 12 month Euribor, but not less than 0, adjusted for yield curve of Bulgarian government securities on primary market according to Bloomberg publication.	N/A	N/A
Loans and advances to customers	1,078,909	722,807	Level 2	Discounted cash flows Future cash flows are measured using the officially published by BNB interest rates, unadjusted, of new loans for December 2018.	N/A	N/A
Receivables from the State budget	497,667	799,661	Level 2	Discounted cash flows Future cash flows are measured using the officially published by BNB yield of Bulgarian government securities, unadjusted, for December 2018	N/A	N/A



Financial instrument	Fair value as of 31.12.2018	Fair value as of 31.12.2017	Fair value hierarchy	Valuation techniques	Significant unobservable inputs	Relationship of unobservable inputs to fair value
Securities held to maturity	13,055	598	Level 2	Discounted cash flows Future cash flows are measured using the officially published by BNB interest rates, unadjusted, of new loans to non-financial entities for December 2018.	N/A	N/A
Other borrowings	110,894	112,299	Level 2	Discounted cash flows Future cash flows are measured using the officially published by BNB yield of Bulgarian government securities, unadjusted, for December 2018	N/A	N/A
Borrowings from international institutions	936,612	899,003	Level 2	Discounted cash flows Future cash flows are measured using the officially published by BNB yield of Bulgarian government securities, unadjusted, for December 2018	N/A	N/A

For the balance sheet assets and liabilities not disclosed in the table the Group's management is of the opinion that their fair value approximates their carrying amount.

6. NET INTEREST INCOME

	2018	2017
Interest income		
Loans and advances to customers	45,926	46,113
Loans to banks	1,707	2,507
Deposits placed with other banks	1,872	945
Financial assets at fair value through other comprehensive income	5,951	3,293
Net investment in finance leases	92	123
Receivables from the State budget	9,254	10,157
Securities at amortised cost	69	52
Other liabilities (income from negative interest)	1,669	88
	66,540	63,278
Incl. Interest income on loans and receivables classified as Phase 3	4,322	4,567
Interest expense		
Borrowings from international institutions	(6,631)	(4,464)
Deposits from customers	(530)	(749)
Deposits from other banks	(4)	(16)
Other borrowings	(124)	(128)
Finance lease	(21)	-
Other assets (expenses on negative interest)	(2,064)	(255)
	(9,374)	(5,612)
Net interest income	57,166	57,666

The yield on the assets, as a ratio of net profit to the balance sheet figure, is 0.91 per cent (2017: 0.84 per cent).

7. NET FEE AND COMMISSION INCOME

	2018	2017
Fee and commission income		
Fee and commission income under IFRS 15		
Services relating to transactions *	1,630	-
Issuance of guarantees and letters of credit	3,945	-
Account maintenance	69	-
Total fee and commission income under contracts with customers	5,644	-
Other charges	35	-
Total fee and commissions 2018	5,679	-
Guarantees and letters of credit	-	3,323
Customers. accounts, bank transfers, cash operations of customers, etc.	-	560

	2018	2017
Fee and commission income		
Servicing of debt issues	-	252
Special-purpose funds of the Ministry of Agriculture and Food and the Executive Agency on Fisheries and Aquaculture (Note 30)	-	679
Special-purpose funds of the Ministry of Finance (Note 30)	-	64
Other	-	32
	-	4,910
Fee and commission expense		
Agency commissions	(34)	(30)
Bank transfers and cash operations with other banks	(4)	(3)
Servicing of accounts in other banks	(31)	(35)
Total fee and commission expenses	(69)	(68)
Net fee and commission income	5,610	4,842

*The transaction-related services include operation on a trust basis of funds of special-purpose funds of the Ministry of Agriculture and Foods and Executive Agency Fisheries and Aquacultures: BGN 1,039 thousand, and of special-purpose funds of the Ministry of Finance: BGN 62 thousand. Further details of the programmes are given in Note 30.

8. NET GAIN ON FOREIGN EXCHANGE DEALS

	2018	2017
Net gain on dealing in foreign currencies	386	419
Net gain on foreign currency translation of assets and liabilities	(7)	(10)
	379	409

9. NET GAIN ON SECURITIES MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

	2018	2017
Net gain on dealing in securities measured at fair value through OCI, incl. realised revaluation reserve	738	188
	738	188

10. OTHER OPERATING INCOME

	2018	2017
Dividends received	17	75
Litigation expenses refunded	843	354
Investment property rentals	871	480
Gain on disposal of assets held for sale	437	197
Gain on disposal of FTAs	1	7
Other income	292	99
	2,461	1,212

11. OTHER OPERATING EXPENSES

	2018	2017
Expenses related to assets held for sale	(280)	(335)
Litigation expenses	(28)	(62)
Withholding tax	(286)	(223)
Direct operating expenses relating to investment property	(204)	(165)
Expenses on disposal of FTAs	(1)	(31)
Other expenses	(993)	(5)
	(1,792)	(821)

12. (EXPENSES ON)/INCOME FROM REVERSED IMPAIRMENT LOSSES AND PROVISIONS

	2018	2017
Expenses on/(Income from/ reversed) impairment of individually significant loans, net	(7,623)	(23,864)
Expenses on/(Income from/ reversed) impairment under unutilised loans	472	-
Income from / (expenses on) reversed impairment on finance lease	(41)	14
(Expenses) / Income on / from reversed guarantee provisions, net	(892)	1,949
Expenses on / (Income from reversed) impairment of assets acquired from collateral foreclosure	(232)	(194)
Expenses on /(Income from reversed) provisions for securities, net	(1,730)	
	(10,046)	(22,095)

The movement in the balance sheet accumulated expenses on impairment and provisions is disclosed in Notes 18, 22, 26 and 31.

13A. COSTS OF PERSONNEL

	2018	2017
Staff remuneration and social security	(11,407)	(9,404)
Remuneration to members of the Management and Supervisory Boards	(2,290)	(2,075)
	(13,697)	(11,479)

	2018	2017
Personnel costs consist of:		
Salaries	(9,945)	(8,121)
Social security	(1,280)	(1,080)
Social benefits	(116)	(104)
Amounts accrued on retirement benefits	(66)	(99)
	(11,407)	(9,404)

13B. GENERAL AND ADMINISTRATIVE EXPENSES

	2018	2017
Contribution to the Bank Resolution Fund (BRF)	(6,913)	(3,180)
Contribution to the Bulgarian Deposit Insurance Fund (BDIF)	(47)	(39)
Rents	(9)	(16)
Communications and IT services	(595)	(560)
Office and office equipment maintenance	(784)	(576)
Legal and consulting services	(271)	(227)
Advertising and entertainment expenses	(898)	(368)
Taxes and government charges	(258)	(219)
Hired services	(488)	(388)
Advisory services by the registered audit firms	(2)	(9)
Business trips	(101)	(67)
Audit services by the registered audit firms	(178)	(148)
	(10,544)	(5,797)

The amounts charges for the year for services provided by the registered audit firms of the Company include: independent financial audit: BGN 178 thousand (2017: BGN 148 thousand), including agreed-upon procedures for BGN 6 thousand (2017: BGN 6 thousand), tax advisory services: BGN 0 (2017: BGN 0), other services not related to audit: BGN 2 thousand (2017: BGN 9 thousand).

14. TAXATION

	2018	2017
Current tax expense	2,078	2,569
Deferred tax benefit due to temporary differences	(434)	(247)
Deferred tax (benefit)/expense due to changes in accounting policies	167	-
Total current tax expense	1,811	2,322

In BGN.000	2018	2017
Accounting profit	28,898	23,002
Income tax calculated at the effective tax rate (10 per cent for 2017, 10 per cent for 2016)	2,890	2 427
Non-deductible expenses	139	34
Non-deductible income	(169)	(139)
Deferred tax (benefit)/expense due to changes in accounting policies	(1,049)	-
Total tax expense	1,811	2,322
Effective tax rate	6,27%	10.10%

Outstanding balances of deferred taxes relate to the following items of the consolidated statement of financial position and changes in the statement of comprehensive income:

	Assets		Liabilities		Changes in the income statement	
	2018	2017	2018	2017	2018	2017
Property and equipment	(15)	(15)	-	-	-	(1)
Other assets	(232)	(444)	-	-	212	35
Guarantee portfolio	-	(290)	-	-	290	121
Other liabilities	(14)	(63)	-	-	49	(11)
Securities	-	(1,446)	-	-	1,446	(448)
Investment property	-	-	-	-	-	57
	(261)	(2,258)	-	-	1,997	(247)

The changes in the temporary differences during the year are recognised in the consolidated statement of comprehensive income.

The probability that the individual differences might reverse in the future and the Group's ability to generate sufficient taxable profit have also been taken into account on recognising deferred tax assets.

15. NET CHANGE IN THE FAI RVALUE OF FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME, NET OF TAXES

	2018	2017
Gain on revaluation of assets at fair value through other comprehensive income occurred throughout the year	(185)	4,281
Income recycling	(158)	188
Other comprehensive income for the year	(343)	4,469

16. CASH IN HAND AND BALANCES IN CURRENT ACCOUNT WITH THE CENTRAL BANK

	2018	2017
Cash in hand	335	244
Current accounts	297,287	447,404
Incl. Minimum statutory reserves	172,143	120,400
Total cash with the Central Bank	297,287	447,404
Total cash in hand and in accounts with the Central Bank	297,622	447,648

The parent company maintains amounts depending on the risk-weighted assets as Minimum statutory reserves with BNB. Deposits with the Central Bank bear interest rate of -0.60 % on the excess over 105% of MRR (2017: - 0,60 %).

17. RECEIVABLES FROM BANKS

In BGN.000	2018	2017
Current accounts and demand deposits with local banks	338	516
Current accounts and demand deposits with foreign banks	14,938	12,512
incl. Current accounts with an original maturity of less than 90 days	4,734	2,485
Term deposits with local banks (incl. repo deals)	244,262	72,013
Term deposits with foreign banks (incl. repo deals)	71,143	-
incl. Term deposits with an original maturity of less than 90 days	315,405	71,786
Loans to local banks	98,971	101,270
Loans to foreign banks	1,467	12,599
Adjustment for impairment and uncollectability of banks	(1,116)	-
	430,003	198,910

At 31 December 2018, special-purpose loans, denominated and BGN and EUR, with original maturity of up to 10 years and interest rate levels ranging from 1.40 per cent to 4.50 per cent (2017: 1.49 per cent to 4.40 per cent), were extended to local banks with the aim to develop small and medium-sized enterprises.

Funds amounting to BGN 10,543 thousand were blocked in current accounts with foreign banks to cover letters of credit (2017: BGN 10,542 thousand).

At 31 December 2018, loans denominated in foreign currency with nominal amount of EUR 5,745 thousand and equivalent to BGN 11,236 thousand were provided to local banks (31 December 2017 – no such loans were extended), with an original maturity until 2027 and repayment of the loans in four instalments. These are special-purpose loans extended to banks for direct lending to customers with the aim to develop small and medium-sized enterprises (SMEs) in accordance with a loan financing by the Ministry of Finance with funds provided by KfW.

18. LOANS AND ADVANCES TO CUSTOMERS

	2018	2017
Loans (gross amount)	1,211,190	867,086
Allowance for impairment and uncollectability of loans	(163,156)	(157,975)
	1,048,034	709,111

	2018	2017
A. Analysis by customer type		
Corporate and sole traders	1,208,029	863,088
Municipalities	928	1,099
Individuals	2,233	2,899
	1,211,190	867,086

	2018	2017
B. Analysis by industry sector depending on the purpose of the loan		
Construction	162,701	146,728
Transport	131,627	106,678
Industry, total	439,267	303,770
Industry – energy generation and distribution	74,714	85,437
Industry – manufacture of foodstuffs	51,392	50,032
Industry – other industries	96,421	46,786
Industry – manufacture of tobacco products	149,129	58,773
Industry – manufacture of plant and equipment	67,611	62,742
Financial services	112,665	69,312
Trade	34,227	38,612
Administrative and office activities	253	49,342
Real estate transactions	49,741	49,475
Agriculture	34,278	33,357

	2018	2017
B. Analysis by industry sector depending on the purpose of the loan		
Government sector	77,659	32,376
Tourist services	108,924	17,342
Other industries	55,658	11,695
Collection and disposal of garbage	4,190	8,399
	1,211,190	867,086

The Bank finance mainly the activities of small and medium-sized enterprises, as well as investment projects to achieve return from 5 to 10 years.

C. Movement in the allowance for loan impairment and uncollectability

In BGN.000	2018			2017		
	Individually impaired	Collectively impaired	Total	Individually impaired	Collectively impaired	Total
At 1 January	157,812	163	157,975	143,135	163	143,298
Effect of IFRS 9	10,019		10,019			
Impairment costs	31,264	-	31,264	43,843	-	43,843
Reversed impairment	(23,731)	(163)	(23,894)	(19,979)	-	(19,979)
Written-off against impairment	(12,208)	-	(12,208)	(9,187)	-	(9,187)
At 31 December	163,156	-	163,156	157,812	163	157,975

19. RECEIVABLES FROM THE STATE BUDGET

	2018	2017
Acquired receivables	-	9,506
Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP)	472,803	728,010
Adjustment for impairment and uncollectability of loans (collective impairment)	(804)	-
	471,999	737,516

At 31 December 2018 (and at 31 December 2017 as well) the receivables classified as Receivables from the State budget – Acquired receivables represent receivables originating from assignment contracts with debtors – secondary budget spending units.

By Decree No. 18 of 2 February 2015, the Council of Ministers of the Republic of Bulgaria approved Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP) (the Programme) on the terms and conditions

for grants award under the Programme and for designating the bodies that will be in charge of its implementation.

The financing under the Programme goes through BDB. For the purpose, the Bank concludes trilateral agreements with regional governors (representatives of the State) and municipal mayors (authorized representatives of the owners' associations).

The parent company is of the opinion that the existing receivables bear a minimal credit risk in so far as the source of the payments is the budget of the Republic of Bulgaria.

The resources attracted by international partners for the purpose of financing the Programme is covered by a State guarantee (see Note 30).

Funds utilised under the Program as of 31 December 2018 amounted to BGN 471,999 thousand (at 31 December 2017: BGN 728,010 thousand).

20. FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

Pursuant to IFRS 9, as of 01 January 2018 the Bank has been reporting a new category of assets in its statement of financial position: financial assets measured at fair value through other comprehensive income.

	2018	2017
Government securities	599,567	-
Corporate bonds	50,808	-
Non-publicly traded companies. shares	2,722	-
Participation in investment program SIA (Note 35)	546	-
Public companies. shares	14	-
	653,657	-

In 2017, these assets were classified under IAS 39 as Assets available for sale.

	2018	2017
Government securities	-	288,881
Non-public companies. shares	-	2,620
Participation in the SIA investment program (note 36)	-	352
Public companies. shares	-	14
	-	291,867

Movement in financial assets measured at fair value through other comprehensive income

	2018	2017
As of 1 January	291,866	-
Additions (purchases)	483,171	-
Disposals (sale and/or maturity)	(121,037)	-

Net increase due to revaluation of securities at fair value through OCI	(343)	-
As of 31 December	653,657	-

Movement in available-for-sale financial assets

	2018	2017
As of 1 January	-	322,965
Additions (purchases)	-	53,258
Disposals (sale and/or maturity)	-	(88,825)
Net increase due to revaluation of available-for-sale securities to fair value	-	4,469
As of 31 December	-	291,867

Financial assets measured at fair value through other comprehensive income comprise mainly government securities with the issuer being the Republic of Bulgaria or other European countries, and corporate bonds.

The non-public companies' shares held by the Group include shares of the European Investment Fund (EIF) amounting to BGN 2,538 thousand. The portion of the nominal value of the acquired shares of EIF, which has not been paid, is due after a decision is taken by the General Meeting of Shareholders of EIF (Note 36).

The remaining portion of the non-public companies' shares amounting to BGN 183 thousand represent shares of the company licensed as a payment system operator under the Bulgarian law – BORICA – Bankservice AD. Only banks can be shareholders of this company and they acquire shares following a specific procedure; the share price is determined using a formula specified in the company's Statute. These shares are presented at cost (acquisition price) due to the fact that at the reporting date there is no sufficiently reliable public information to determine an actual fair value of these shares.

The reserve formed on financial assets at fair value through OCI as of 31 December 2018 amounts to BGN 10,909 thousand – a positive value (31 December 2017: BGN 11,003 thousand – a positive value) (Note 34).

In 2018, there was no transferred or reported allowance for impairment of assets measured through other comprehensive income in current profit or loss for the year) (Note 9) (2017: there was no transferred and reported impairment of available-for-sale securities in the statement of comprehensive income).

21. SECURITIES HELD TO MATURITY

	2018	2017
Corporate bonds of financial entities	-	594
	-	594

Corporate bonds of financial entities represent bonds issued by a Bulgarian company denominated in EUR with nominal value EUR 1,000 thousand.

22. NET INVESTMENT IN FINANCE LEASES

The net investment in finance lease is the difference between the gross investment in the finance lease, less any unearned finance income, and the accumulated impairment losses.

	2018	2017
Gross investment in finance leases	1,577	1,705
Unearned finance income	(159)	(212)
Net minimum lease payments	1,418	1,493
Impairment loss	(486)	(458)
Net investment in finance lease	932	1,035

Allocation of net finance lease investment:

	2018	2017
Repayment not later than one year	34	41
Repayment later than one year and no later than five years	1,384	1,452
Net minimum lease payments	1,418	1,493
Impairment loss	(486)	(458)
Net investment in finance lease	932	1,035

The accrued and not yet matured interest as at the date of the financial statements amount to BGN 5 thousand (2017: BGN 7 thousand).

Movement in the allowance for impairment:

	2018	2017
Balance as of 1 January	(458)	(474)
Effect from the first-time adoption of IFRS 9	8	
Impairment over the year:		
Charge for the year	(48)	(11)
Reversed for the year	7	25
Written off	5	2
Balance as of 31 December	(486)	(458)

23. PROPERTY, PLANT AND EQUIPMENT, INTANGIBLE ASSETS

	Land and buildings	Bank equipment and computers	Fixtures and fittings	Motor vehicles	Licences and software	Total
Book value						
As of 1 January 2017	32,553	2,277	618	363	1,187	36,998
Additions	-	196	181	-	133	510
Disposals	-	(347)	(221)	-	(5)	(573)
As of 31 December 2017	32,553	2,126	578	363	1,315	36,935
Acquired as part of business combination (08 June 2018)	4,558	13	20	-	112	4,703
Additions	121	28	126	775	224	1,274
Disposals	-	(18)	(56)	-	-	(74)
As of 31 December 2018	37,232	2,149	668	1,138	1,651	42,838
Accumulated depreciation						
As of 1 January 2017	721	1,124	261	174	939	3,219
Charge for the year	576	324	58	64	102	1,124
Disposals	-	(322)	(80)	-	(5)	(407)
As of 31 December 2017	1,297	1,126	239	238	1,036	3,936
Charge for the year	768	286	77	142	104	1,377
Disposals	-	(16)	(56)	-	-	(72)
As of 31 December 2018	2,065	1,396	260	380	1,140	5,241
Carrying amount						
As of 31 December 2018	35,167	753	408	758	511	37,597
As of 31 December 2017	31,256	1,000	339	125	279	32,999

The fully depreciated property, plant and equipment still in use at 31 December 2018 amount to BGN 1,122 thousand at cost (2017: BGN 25 thousand) and intangible assets amount to BGN 837 thousand (2017: BGN 799 thousand) respectively.

24. INVESTMENT PROPERTY

	2018	2017
Carrying amount at the beginning of period	7,702	7,702
Reclassified from held for sale	-	-
Sold	(53)	-
(Loss) on change in the fair value included in profit and loss for the period	-	-
	7,649	7,702

The Group holds investment properties as a result of collateral acquired on problem loans. They are leased to third parties. Rental income generated for 2018 amounts to BGN 594 thousand (2017: BGN 480 thousand) (Note 10). The fair value at 31 December 2018 has been determined by an independent certified appraiser.

The Group classifies its investment property in Level 3 of the fair value hierarchy. The fair value has been determined on the basis of the valuation calculated by independent certified appraisers by employing valuation techniques and key inputs for the valuation of the investment property disclosed in Note 5.

25. ASSETS HELD FOR SALE

Properties (land, buildings and fixtures and fittings) at 31 December 2018 amounting to BGN 5,012 thousand (2017: BGN 10,100 thousand – land and buildings) were acquired by the Group in 2018 against payment of liabilities under problem loans of borrowers.

The assets have not been used and it is not planned to be used in the Group's activity. Management actively seeks buyers with the purpose to sell them by the end of 2019.

Movement in assets held for sale in 2018 and 2017:	2018	2017
Carrying amount at the beginning of period	10,100	4,670
Acquired from collateral foreclosure	4,835	9,582
Sold	(956)	(2)
Reclassified to other assets	(8,963)	-
Reclassified to assets acquired from collateral foreclosure	-	(4,150)
Impairment	(4)	-
	5,012	10,100

26. OTHER ASSETS И ASSETS ACQUIRED FROM COLLATERAL FORECLOSURE

	2018	2017
Assets acquired from collateral foreclosure	27,128	15,875
Other receivables	908	727
VAT refundable	545	439
Income tax overpaid	-	1,596
Prepayments and advances	156	224
	28,737	18,861

Assets acquired from collateral foreclosure include assets acquired by the Group as a result of non-performing loans. These assets are measured at the lower of cost and net realisable value. The net realisable value is determined based on evaluations made by licensed independent valuers; management considers these evaluations reasonable and adequate for the Group

	2018	2017
Movement in assets acquired from collateral foreclosure in 2018 and 2017:		
Carrying amount at the beginning of period	15,875	11,372
Reclassified from assets held for sale	8,963	4,150
Expenses on construction	3,096	1,341
Sold	(575)	(794)
Impairment	(231)	(194)
Carrying amount at the end of period	27,128	15,875

27. DEPOSITS FROM CREDIT INSTITUTIONS

	2018	2017
Deposits from local banks	4,323	32,361
Deposits from foreign banks	1,436	1,548
	5,759	33,909

There were no interest payable on deposits from credit institutions as at 31 December 2018 (2017: BGN 12 thousand).

	2018	2017
Term deposits	-	30,012
Demand deposits	5,759	3,897
	5,759	33,909

28. DEPOSITS FROM CUSTOMERS OTHER THAN CREDIT INSTITUTIONS

	2018	2017
Individuals	5,198	8,268
Companies and sole traders	1,166,627	651,579
	1,171,825	659,847

The amounts due to individuals represent deposits of employees of the Group.

Interest payable on deposits from other customers, other than credit institutions, at 31 December 2018 amounts to BGN 539 thousand (2017: BGN 156 thousand).

	2018	2017
Term deposits	492,235	75,309
Demand deposits	679,590	584,538
	1,171,825	659,847

29. BORROWINGS FROM INTERNATIONAL INSTITUTIONS

	2018	2017
Long-term framework loan agreement with the Council of Europe Development Bank	277,271	325,929
Long-term loans from the European Investment Bank	146,722	146,721
Long-term loans from the Nordic Investment bank	11,947	16,521
Long-term loans from the Kreditanstalt für Wiederaufbau	154,223	195,667
Sumitomo Mitsui Banking Corporation Europe	-	-
The Export – Import Bank of China	97,727	-
		-
Long-term loans from the Japanese Bank for International Cooperation	-	969
European Investment Fund	1,712	7,859
Industrial and Commercial Bank of China	-	19,660
China Development Bank	215,180	156,496
	904,782	869,822

The outstanding interest on the borrowings from international institutions as of 31 December 2018 amounts to BGN 755 thousand (2017: BGN 924 thousand).

The effective interest rates on borrowings from international institutions as of 31 December 2018 range from 0% to 1.75% (31 December 2017: from 0% to 3.39%).

Council of Europe Development Bank

On 18 November 2009, a loan agreement was signed between Bulgarian Development Bank AD and the Council of Europe Development Bank (CEB) for EUR 15,000 thousand. The purpose of the loan is to finance investment projects of micro-, small and medium-sized enterprises from the real sector with the aim to create new and to preserve already existing jobs. The loan is unsecured.

As of 31 December 2018, the loan was fully utilised and the outstanding principal under the facility amounted to EUR 3,750 thousand equivalent to BGN 7,334 thousand (31 December 2017: EUR 5,625 thousand equivalent to BGN 11,002 thousand). The interest rate is floating, based on the 3M EURIBOR plus a margin.

On 30 March 2011, a new loan agreement was signed between Bulgarian Development Bank AD and the Council of Europe Development Bank for EUR 20,000 thousand. The purpose of the loan is to improve the access to financing of the Bulgarian small and medium-sized enterprises, to create new jobs, and to preserve already existing ones. The loan is unsecured.

As of 31 December 2018, the loan was fully utilised and the outstanding principal under the facility amounted to EUR 9,000 thousand equivalent to BGN 17,602 thousand (31 December 2017: EUR 11,000 thousand equivalent to BGN 21,514 thousand). The interest rate on the first tranche is floating, based on the 3M EURIBOR plus a margin, and on the second tranche it is fixed.

On 23 February 2016, Bulgarian Development Bank signed a Loan agreement with the Council of Europe Development Bank (CEB) amounting to EUR 150,000 thousand. The funds have been used to finance energy efficiency and retrofitting measures under Energy Efficiency of Multi-Family Buildings National Programme (EEMF-

BNP). The loan has a special purpose and has been used for renovation of multi-family buildings. The repayment period of the loan is up to 10 years. As of 31 December 2018, the loan was fully utilised.

The loan is secured by a State guarantee under the State Budget of the Republic of Bulgaria Law for 2016. A Guarantee Agreement was signed between the CEB and the Republic of Bulgaria, represented by the Minister of Finance, which was ratified by the National Assembly. The Guarantee Agreement Ratification Act was promulgated in State Gazette on 3 May 2016.

The Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP) was approved by virtue of decision of the Council of Ministers of 27 January 2015.

As of 31 December 2018, the outstanding principal under the loan amounted to EUR 129,000 thousand, equivalent to BGN 252,302 thousand (as of 31.12.2017: EUR 150,000 thousand equivalent to BGN 293,375 thousand). The interest rate on the first tranche of the loan is floating, based on 3M EURIBOR plus a margin, and on the second tranche it is fixed.

European Investment Bank

On 18 November 2016, BDB signed a contract with European Investment Bank for the amount of EUR 150,000 thousand for financing of projects of small and medium-sized enterprises. The funds are provided with the support of the EU and are backed by an EFSI (European Fund for Strategic Investment) guarantee, part of the Investment Plan for Europe – the Juncker Plan. The funds will be used to finance SMEs, including innovative projects, to support regions with high unemployment rates, as well as youth employment or start-up company projects. The loan can be allocated through partner banks, other financial intermediaries or directly. The loan is unsecured.

As of 31 December 2018, the outstanding principal under the loan amounted to EUR 75,000 thousand equivalent to BGN 146,687 thousand (as at 31 December 2017: EUR 75,000 thousand equivalent to BGN 146,687 thousand). The interest rate is floating, based on the 6M EURIBOR plus a margin.

Kreditanstalt für Wiederaufbau

On 27 July 2010, Bulgarian Development Bank AD signed a direct loan agreement for EUR 25,000 thousand with the German Development Bank Kreditanstalt für Wiederaufbau (KfW). The purpose of the loan is direct lending to small and medium sized enterprises and/or for providing credit lines to commercial banks for special-purpose business financing. The loan is unsecured. At 31 December 2018, the loan was fully utilised.

As of 31 December 2018, the outstanding principal under the facility amounted to EUR 5,882 thousand equivalent to BGN 11,505 thousand (at 31 December 2017: the outstanding principal amounted to EUR 8,824 thousand equivalent to BGN 17,257 thousand). The interest rate is floating, based on the 6M EURIBOR plus a margin.

On 16 August 2016, Bulgarian Development Bank signed an Agreement with KfW for EUR 100,000 thousand. The funds will be used to finance energy efficiency and retrofitting measures, implemented by SMEs in Bulgaria under the Energy Efficiency of Multi-Family Buildings National Programme (EEMFBNP) The loan is secured by a State guarantee under the State Budget of the Republic of Bulgaria Law for 2016. A Guarantee Agreement was signed between KfW and the Republic of Bulgaria, represented by the Minister of Finance, which was ratified by the National Assembly. The Guarantee Agreement Ratification Act was promulgated in State Gazette on 30 December 2016. The repayment period of the loan is 7 years, with a grace period of 2 years. As of 31 December 2018, the loan was fully utilised.

As of 31 December 2018, the outstanding principal under the facility amounted to EUR 72,727 thousand equivalent to BGN 142,242 thousand (as of 31 December 2017, the outstanding principal under the facility amounted

to EUR 90,909 thousand equivalent to BGN 177,803 thousand). The interest rate is floating, based on the 6M Euribor plus a margin.

Nordic Investment Bank

On 15 December 2010, a second credit line was signed between the Nordic Investment Bank and Bulgarian Development Bank AD for EUR 20,000 thousand. The purpose of the loan is financing of renewable energy projects or environmental projects; projects involving the Nordic Investment Bank member states, as well as indirect financing through commercial partner banks. The loan is unsecured. As of 31 December 2018, the loan was fully utilised.

As of 31 December 2018, the outstanding principal under the facility amounted to EUR 6,136 thousand equivalent to BGN 12,001 thousand (31 December 2017: EUR 8,489 thousand equivalent to BGN 16,603 thousand). The interest rate is floating, based on 6M EURIBOR plus a margin.

Sumitomo Mitsui Banking Corporation Europe

On 11 November 2014, BDB signed a new agreement with Sumitomo Mitsui Banking Corporation Europe for trade financing of commercial transactions and letters of credit, including export deals, with a term of up to 12 months. The agreement is for EUR 10,000 thousand.

At 31 December 2018, there was no outstanding principle under the loan (31 December 2017: no outstanding principle). The interest rate is floating, based on EURIBOR plus a margin.

Japan Bank for International Cooperation (JBIC)

On 17 December 2009, a Loan agreement was signed between Bulgarian Development Bank AD and Japan Bank for International Cooperation for EUR 20,000 thousand. The purpose of the loan is financing of Japanese projects and can be utilised in EUR or JPY. For a loan in EUR the applicable interest rate is fixed (CIRR plus risk margin) for 60 per cent of the amount and floating (6M EURIBOR + margin) for the rest 40 per cent. For a loan in JPY the applicable interest rate is fixed (CIRR plus risk margin). The loan is unsecured. The utilised amount under the loan is JPY 1,122,594 thousand equivalent to BGN 19,812 thousand.

As of 31 December 2018, the loan was fully paid (31 December 2017: JPY 70,149 thousand equivalent to BGN 1,016 thousand).

Progress Program of the European Investment Fund

On 24 July 2015, a loan agreement was signed between Bulgarian Development Bank AD and the Progress Program of EIF for EUR 5,000 thousand. The purpose of the loan is to finance micro-leases and micro-loans for micro and small enterprises, as well as to finance micro-loans through financial institutions. This Program targets companies with up to 10 employees and assets up to EUR 2 million (BGN 3,912 thousand). Self-employed persons, start-ups, or persons experiencing difficulties in obtaining financing are also eligible as beneficiaries.

As of 31 December 2018, the loan principal due amounted to EUR 871 thousand equivalent to BGN 1,704 thousand (31 December 2017: EUR 4,000 thousand equivalent to BGN 7,823 thousand). The interest on the loan is fixed.

Industrial and Commercial Bank of China (ICBC)

On 22 February 2016, BDB signed an inter-bank loan agreement with ICBC for EUR 20,000 thousand. The purpose of the loan is financing of the general lending activity of BDB, direct business financing or on-lending through commercial banks for investment projects and working capital. The term of the loan is two years. The loan is unsecured. As of 31 December 2018, the loan was fully paid (31 December 2017: EUR 10,000 thousand equivalent to BGN 19,558 thousand).

China Development Bank

On 12 May 2017, BDB signed a loan agreement with China Development Bank for the amount of EUR 80,000 thousand. The purpose of the loan is financing the general lending activity of BDB – investment and working capital loans. BDB could also use the funds to support strategic projects within the Belt & Road initiative. The tenor of the loan is 10 years, with a 2-years grace period. The loan is unsecured. As of 31 December 2018, the loan was fully utilized.

As of 31 December 2018, the outstanding principal under the loan amounted to EUR 80,000 000 thousand equivalent to BGN 156,466 thousand (as of 31 December 2017: EUR 80,000 000 thousand equivalent to BGN 156,466 thousand). The interest rate is floating based on the 6M EURIBOR plus a margin.

On 13 December 2018, BDB signed a new financing agreement with the China Development Bank amounting to EUR 300,000 thousand. The funds were granted as a first tranche under the framework agreement signed in July 2018 for EUR 1.5 billion. The funds may be used to finance projects within the Belt & Road initiative and/or projects in support of SMEs, energy, communications, transport, agriculture in Bulgaria or for other purposes agreed by BDB and CDB. The term of the contract is 10 years.

As of 31 December 2018, the outstanding principal under the loan amounted to EUR 30,000 thousand equivalent to BGN 58,675 thousand (as of 31 December 2017: no amounts due under the loan). The interest rate is floating based on the 6M EURIBOR plus a margin.

The Export – Import Bank of China

On 28 September 2017, BDB signed an agreement with the Export – Import Bank of China for the amount of EUR 50,000 thousand. This was the first loan agreement between BDB and the Export – import Bank of China, following the financial cooperation agreement, signed in 2014 between the two institutions and setting their interest in joint financing of key projects or areas. The funds can be used to finance the overall lending activity of BDB, a short-term and mid-term trade financing, trans-border economic and commercial transactions between China and Bulgaria. The loan tenor is 5 years. The loan is unsecured.

As of 31 December 2018, the loan was fully utilised; the outstanding principal under the loan amounted to EUR 50,000 thousand equivalent to BGN 97,792 thousand (31 December 2017: no amounts were utilised under the loan). The interest rate is floating based on the 6M EURIBOR plus a margin.

30. OTHER BORROWINGS

	2018	2017
Loan financing from the Ministry of Finance with funds from KfW	11,236	11,236
KfW funds provided by the Ministry of Finance for trust management	6,070	6,256
Special-purpose deposits	93,025	93,914
	110,331	111,406

There were no interest liabilities accrued on other borrowings as of 31 December 2018 (2017: Nil).

Loan financing from the Ministry of Finance with funds from KfW

On 18 April 2007, the Bank concluded a loan agreement with the Government of the Republic of Bulgaria, represented by the Minister of Finance. This agreement is based on the Treaty between Bulgaria and Germany for financial collaboration from 2001 and an Agreement between the Republic of Bulgaria and Kreditanstalt für Wiederaufbau (KfW). By virtue of this agreement, the amount of EUR 4,929 thousand (BGN 9,640 thousand) is granted to the Bank designated as Project Promoter for the purpose of financing micro, small and medium-sized enterprises. The term of the agreement is 10 years as from the date of transfer of the funds, while the latter along with the due interest shall be repaid bullet at the end of the period.

On 28 April 2017, BDB and the Ministry of Finance signed Annex 1 to extend the term of the contract by 10 more years.

As of 31 December 2018, the outstanding principal and the capitalised interest amounted to EUR 5,745 thousand equivalent to BGN 11,236 thousand (as of 31 December 2017: EUR 5,745 thousand equivalent to BGN 11,236 thousand).

The loan interest is capitalised quarterly and is based on 3M EURIBOR plus a margin.

As of 31 December 2018, the Bank has extended under this contract loans to commercial banks amounting to EUR 5,745 (31 December 2017: no funds were extended).

KfW funds provided by the Ministry of Finance for trust management

The Bank has concluded an agreement with the Ministry of Finance (MF) for management of funds granted by Kreditanstalt für Wiederaufbau (KfW) pursuant to an agreement between the Governments of Bulgaria and Germany. These funds are provided for financing of small and medium-sized enterprises. The Ministry of Finance bears the risk under the loans to partner-banks. The Bank selects the partner-banks and transfers the funds to those approved; gathers information and performs periodic reviews of the funds utilisation, monitors the timely interest and principal payments to the special account of the Ministry of Finance.

As of 31 December 2018, the outstanding principal of the funds under trust management with the parent company (the Bank) amounts to EUR 3,104 thousand equivalent to BGN 6,070 thousand (31 December 2017: EUR 3,199 thousand equivalent to BGN 6,256 thousand).

The Bank receives a management fee and accrues interest on the special account of the Fund on a quarterly basis.

Long-term agreement with the Executive Agency on Fisheries and Aquaculture

On 07 December 2010 a financing agreement for provision of funds for the issuance of guarantees under the Operational programme for development of fisheries sector 2007-2013 was signed between the National Guarantee Fund (NGF) and the Executive Agency on Fisheries and Aquaculture (NAFA) of the Ministry of Agriculture and Food of the Republic of Bulgaria. The aim of the program is to provide easier access to financing by the sector, with lower interest rates, lower collateral requirements and lower own financing.

The guarantee program is fulfilled within the Measure 2.7 of the Rural Development (RDP) Programme. Following consultations, the Executive Agency on Fisheries and Aquaculture (NAFA) and NGF EAD have chosen the financial engineering instrument, provided for under Commission Regulation (EC) No.498/2007 (OB, 10.05.2007, L 120) laying down detailed rules for the implementation of Council Regulation (EC) No.1198/2006, to be realised through a fund (accounts) in an account and under the governance of NGF.

In accordance with Commission Regulation (EC) No.498/2007 (Article 35), the financial engineering instrument is established in the form of a separate financial pool within NGF EAD.

In 2010, NAFA provided to NGF the amount of BGN 6,000 thousand under Article 1 of the Financing Agreement. On 28 December 2011 pursuant to Annex 2 an additional contribution of BGN 9,168 thousand was made. On 19 December 2012 Annex 4 of the Financing Agreement for provision of funds for the issuance of guarantees under the Operational programme for development of fisheries sector 2007-2013 was signed between NGF and NAFA. Pursuant to Annex 4, NAFA shall transfer to NGF additional contribution amounting to BGN 15,050 thousand for the realisation of the guarantee scheme. In accordance with Annex 5 signed between NGF EAD and NAFA on 16 January 2014, the Agency has withdrawn the last contribution of BGN 15,050 thousand. By Annex No. 7 dated 06 October 2015 between the parties, the Fund refunded to the Agency the amount of BGN 3,000 thousand from the additionally transferred financial resources.

By Annex 8 dated 03 November 2017, the parties expressed their intention to reuse the resources. NAFA assigned NGF EAD with the task to carry out Guarantee activity in favour of micro-, small-, and medium-sized enterprises operating in the Fisheries sector in accordance with article 34, paragraph 4 of Regulation (EC) 498/2007.

By Annex 9 dated 19 June 2018, the parties declared that the funds provided under the Agreement would be reused by the National Guarantee Fund in activities aiming to facilitate the access to financing of Fisheries sector enterprises and enterprises approved to receive grant under the Maritime and Fisheries Programme 2014 -2020. The funds have been granted to finance Guarantee activities for a ten-year term.

In 2015, aiming at achieving a better yield, the program funds were invested in a current account bearing a preference interest rate with Bulgarian Development Bank AD. In 2016, the funds were deposited in a two-year deposit with the same bank. In 2017, the deposit agreement was annexed for three more years.

The guarantee program is free of charge for businesses that benefit from it, while the cost for NGF EAD for its realisation are determined and paid under Article 35 of Commission Regulation (EC) No.498/2007.

As of 31 December 2018, within the OPRDP, NGF EAD has signed agreements with the following banks: Raiffeisenbank (Bulgaria) EAD, First Investment Bank AD, UBB EAD, UniCredit Bulbank AD, Central Cooperative Bank AD, DSK Bank EAD, TBI Bank EAD, International Asset Bank AD, Bulgarian American Credit Bank AD, and Bulgarian Development Bank AD, Municipal Bank AD.

The term for inclusion of new loans and bank guarantees (which are scheduled within the Program) matures on 31 December 2022.

Long-term agreement with the Ministry of Agriculture and Food

On 20 December 2011, the National Guarantee Fund EAD and the Ministry of Agriculture and Food (MAF) signed a financial agreement to provide funds for the implementation of guarantees on guarantee schemes under the Rural Development Programme 2007 – 2013.

The Guarantee Scheme was established on the grounds of Articles 51 – 52 of Commission Regulation (EC) No. 1974/2006 dated 15 December 2006 laying down detailed rules for the implementation of Council Regulation (EC) No. 1698/2005 dated 20 September 2005 regarding the support for rural development under EAFRD to facilitate access to financing of beneficiaries and the realisation of the projects under OPRDP.

MAF provides funding to NGF in BGN amount equivalent to EUR 121,100 thousand (BGN 242,000 thousand), in order to enhance the access to financing, support competitiveness, accelerate the completion of investments, which will be co-finance with funds under the Rural Development Programme (2007-2013) and which are used by the Fund for the issuance of guarantees and counter-guarantees. By Annex No. 2 dated 14 October 2015 signed between the parties, the Fund refunded to the Ministry the amount of BGN 154,586 thousand from the financial resources provided. By Annex No. 3 dated 01 December 2015, signed between the parties, the term of the Agreement was extended until 01 April 2016.

Pursuant to Annex No. 4 dated 29 March 2016 the parties declared that the funds provided under the Agreement should be re-used by the Guaranteed Activity Fund with the aim to facilitate access to financing for entities approved for aid under the Rural development programme of the Republic of Bulgaria (2014-2020 e.), as also for entities from Livestock breeding sector and Plant production sector. The funds are provided for carrying out guaranteed activities for a term of ten years.

In 2016 the funds were placed in a two-year deposit with the parent company. In 2017, the deposit agreement was annexed for three more years.

As of 31 December 2017, within the Guarantee Scheme under OPRDP 2007 – 2013, NGF EAD has concluded agreements with the following banks: Bulgarian American Credit Bank AD, DSK Bank EAD, United Bulgarian Bank AD, Piraeus Bank Bulgaria AD, First Investment Bank AD, Raiffeisenbank (Bulgaria) EAD, Cibank EAD, Central Cooperative Bank AD and Eurobank Bulgaria AD, UniCredit Bulbank AD, TBI Bank EAD, and Allianz Bank Bulgaria AD.

In 2017, the Guarantee Scheme 2014 -2020, a joint activity with MAF, was implemented by using funds amounting to BGN 50,000 thousand, released from the Guarantee Scheme under OPRDP 2007 – 2013. New agreements under the Guarantee Scheme was signed with 17 commercial banks: United Bulgarian Bank AD, Texim Bank AD, DSK Bank EAD, Piraeus Bank Bulgaria AD, Cibank EAD, Bulgarian American Credit Bank AD, Municipal Bank AD, Investment Bank AD, Allianz Bank Bulgaria AD, International Asset Bank AD, Eurobank Bulgaria AD, D Commercial Bank AD, TBI Bank EAD, First Investment Bank AD, UniCredit Bulbank AD, Bulgarian Development Bank AD, Raiffeisenbank (Bulgaria) EAD, and MFI Jobs EAD.

31. PROVISIONS

	2018	2017
Guarantee provisions	7,641	5,759
Provisions for unutilised loans	187	97
	7,828	5,856

The movement in guarantee provisions is presented in the following table:

	2018	2017
Balance as of 1 January	5,794	7,509
Effect from the first-time adoption of IFRS 9 on 01 January 2018	449	-
Charged over the year	2,229	1,982
Utilised over the year	3,721	198
Reversed over the year	(4,552)	(3,930)
Balance as of 31 December	7,641	5,759

Guarantee provisions consist of the amount the Group estimates as highly probable to be required to be actually paid to third parties under guarantees issued by the Group.

Litigation provisions relate to future payments under lawsuits relating to labour disputes.

32. OTHER LIABILITIES

	2018	2017
Charges on bonds and portfolio guarantees	48	196
Payables to personnel and for social security	591	454
Retirement benefit liabilities	400	366
Accruals for expenses	365	777
Taxes payable	367	281
Payables to EIF	5	148
Finance lease liabilities	561	-
Other creditors	443	617
	2,780	2,839

Payables to personnel for salaries and social security contributions comprise accruals on compensated absences and social security contributions due thereon.

Employee retirement benefits are due by the Group to employees reaching retirement age and are stated at their present value.

In accordance with the Labour Code each employee is entitled to indemnity on retirement amounting to two gross monthly salaries, and if he / she has worked for more than 10 years for the parent company (the Bank) – to six gross monthly salaries at the time of retirement. The parent company (the Bank) estimated the amount of these liabilities by using mathematical models and the services of a certified actuary. On the basis of the calculations made, the amount of BGN 400 thousand was included in the consolidated statement of financial position at 31 December 2018 (31 December 2017: BGN 336 thousand).

	2018	2017
Present value of the liability at 1 January	366	229
Current service cost	101	49
Interest expense	6	7
Amounts paid in the period	(19)	-
Actuarial (gains)/losses from changes in demographic and financial assumptions and actual experience	(54)	81
Present value of the liability at 31 December	400	366

	Amounts on retirement for old age and length of service		Amounts on retirements due to illness		Total	
	2018	2017	2018	2017	2018	2017
Actuarial gain/(loss) at 1 January	(41)	22	-	-	(41)	22
Actuarial (loss)/ gain recognized in other comprehensive income for the period	33	(63)	-	-	33	(63)
Actuarial (loss)/gain at 31 December	(8)	(41)	-	-	(8)	(41)

The following actuarial assumptions are used in calculating the present value of the liabilities as of 31 December 2018:

- mortality rate – in accordance with the table prepared on the basis of statistics issued by the National Statistical Institute for the total mortality rate of the population in Bulgaria for the period 2015 – 2017;
- staff turnover rate – from 0 per cent to 10 per cent depending of five age groups formed;
- rate of early retirement due to illness – from 0.027 per cent to 0.3212 per cent depending of five age groups formed;
- effective annual interest rate for discounting – 1 per cent (2017: 1.4 per cent);
- assumptions for the future level of working salaries in the Bank are based on the parent company.s (Bank.s) development plan for 2019 – 5 per cent compared to the 2018 level and for 2020 and subsequent years – 5 per cent compared to the previous year level.

The effect for 2018 of the increase and decrease by 1 per cent of the salary growth and the interest rate on the total amount of current service costs and interest, and on the present value of the liability for payment of defined benefits upon retirement, are as follows:

	Increase by 1% of salary growth	Decrease by 1% of salary growth
Change in the interest and current service costs ("+" – increase, "-" – decrease)	17	(14)
Change in the present value of the liability as of 31 December 2018 ("+" – increase, "-" – decrease)	60	(49)

	Increase by 1% of interest rate	Decrease by 1% of interest rate
Change in the interest and current service costs ("+" – increase, "-" – decrease)	(9)	12
Change in the present value of the liability as of 31 December 2018 ("+" – increase, "-" – decrease)	(50)	62

	Increase by 1% of staff turnover rate	Decrease by 1% of staff turnover rate
Change in the interest and current service costs ("+" – increase, "-" – decrease)	(15)	19
Change in the present value of the liability as of 31 December 2018 ("+" – increase, "-" – decrease)	(53)	65

The effect for 2017 of the increase and decrease by 1 per cent of the salary growth and the interest rate on the total amount of current service costs and interest, and on the present value of the liability for payment of defined benefits upon retirement, are as follows:

	Increase by 1% of salary growth	Decrease by 1% of salary growth
Change in the interest and current service costs ("+" – increase, "-" – decrease)	13	(11)
Change in the present value of the liability as of 31 December 2018 ("+" – increase, "-" – decrease)	52	(43)

	Increase by 1% of interest rate	Decrease by 1% of interest rate
Change in the interest and current service costs ("+" – increase, "-" – decrease)	(7)	9
Change in the present value of the liability as of 31 December 2018 ("+" – increase, "-" – decrease)	(44)	54

	Increase by 1% of staff turnover rate	Decrease by 1% of staff turnover rate
Change in the interest and current service costs ("+" – increase, "-" – decrease)	(12)	14
Change in the present value of the liability as of 31 December 2018 ("+" – increase, "-" – decrease)	(46)	56

33. SHARE CAPITAL

	2018	2017
Share capital		
Ordinary shares issued paid in cash	587,964	587,964
Ordinary shares issued – in-kind contribution (land for the building of the bank)	12,200	12,200
Ordinary shares issued – in-kind contribution (the building of the bank)	1,610	1,610
	601,774	601,774

The capital of the parent company (the Bank) is composed by 6,017,735 ordinary registered voting shares with par value of BGN 100 each.

The Bulgarian Development Bank Act provides that not less than 51 per cent of shares forming the Bank's capital should be owned by the State; the shares of the State amounting to not less than 51 per cent of the registered share capital are non-transferable. Also, a specific limit is established with regard to the remaining shareholders, other than the Bulgarian State through the Ministry of Finance. Shareholders may be: the Council of Europe Development Bank, the European Investment Bank, the European Investment Fund as well as other banks for development in EU member states.

The Bank's shares may not be pledged and the rights thereon may not be subject to transfer deals.

In August 2017, by decision of the SB, the Bank's shares were transferred from the Ministry of Finance to the Ministry of Economy and as of 31 December 2018, 99.99 per cent of the Bank's shares were held by the State through the Ministry of Economy (31 December 2017: 99.99 per cent of the Bank's shares were held by the State through the Ministry of Finance).

34. RESERVES

In accordance with the general provisions of the Commercial Act, the parent company (the Bank) shall allocate to Reserve Fund at least 1/10 of its profit for the year until the reserves reach 10 percent of the share capital as stipulated in the Articles of Association. Pursuant to the Articles of Association of the Bank, the Bank shall set aside to the Reserve Fund at least 1/2 of its after-tax annual profit until the reserves reach 50 percent of its share capital.

The Reserve Fund may be used by the Group only to cover its current or prior period losses, and not for distribution of dividends, without the authorisation of Bulgarian National Bank.

Moreover, the Credit Institutions Act stipulates that the banks in Bulgaria cannot distribute dividends before accumulating the minimum reserves (mainly the Reserve Fund) required by law or by their Articles of Association, or if the distribution of dividends will result in violation of the regulatory capital adequacy ratios. The requirement under the Bulgarian Development Bank Act is similar.

As of 31 December 2018, the Reserve Fund of the Group amounted to BGN 73,672 thousand. (31 December 2017: BGN 71,989 thousand).

As of 31 December 2018, the Additional Reserves of the Bank amounted to BGN 77,324 thousand (31 December 2017: BGN 68,063 thousand) and were formed as result of distribution of profits of the Bank from previous periods, according to decisions of the General Meeting of Shareholders.

In 2018, after a regular General Meeting of Shareholders of the Bank a decision was passed not to distribute dividends against the profit net of the contribution to the Reserve Fund (2017: dividend of BGN 19,314 thousand was paid against the profit).

In accordance with the Bulgarian Development Bank Act, each shareholder of the Bank is allowed to waive the right to a dividend and then the dividend amount is transferred to Additional Reserves.

All unrealised gains and losses on fair value revaluation of the financial assets measured at fair value through other comprehensive income held at the end of each reporting period are recognised in equity, in a special components thereof formed by the Group and titled Reserve for financial assets measured at fair value through other comprehensive income. These gains and losses are transferred to current profits and losses upon sale/maturity of the respective securities and/or on permanent impairment. The financial assets at fair value through other comprehensive income reserve is presented net of taxes. As of 31 December 2018, the reserve is a positive value amounting to BGN 10,909 thousand (31 December 2017: BGN 11,003 thousand – positive value).

35. CONTINGENCIES AND COMMITMENTS

	2018	2017
Contingent liabilities		
Guarantees and letters of credit	484,134	407,746
incl. with cash collateral	(15,539)	(9,472)
Letters of credit with borrowed funds, accounted as loan commitment	-	21
Guarantee provisions (Note 31)	(7,641)	(5,829)
	460,954	392,466
Risk free counter guarantees issued	-	63,696
Irrevocable commitments		
Unutilised amount of approved loans	328,324	446,223
incl. letters of credit with borrowed funds	-	(21)
Unclaimed portion of par value of EIF shares	4,694	4,694
Participation in the SIA investment program	1,410	1,603
	334,428	452,499
	795,382	844,965

Pursuant to the Bulgarian Development Bank Act, the transfers of activities under the Micro-credits Guarantee Fund Project from the Ministry of Labour and Social Policy (MLSP) to the National Guarantee Fund EAD – subsidiary of the Bank began in the last quarter of 2008. Based on the law and on Council of Ministers Decision No. 309/3 May 2007, re-negotiations were carried out within one year (until May 2009) with each of the partner banks to the Micro-credits Guarantee Fund Project of MLSP for replacing the security of MLSP deposits with bank guarantees of Bulgarian Development Bank AD. The capital of Bulgarian Development Bank AD and respectively, of National Guarantee Fund, was increased with the amount of the government funds released under the project.

As of 31 December 2018, agreements with five partner banks were concluded by the parent company (the Bank) and bank guarantees amounting to BGN 1,551 thousand (31 December 2017: five partner banks and bank guarantees issued amounting to BGN 1,818 thousand) were issued.

On 17 July 2015, Bulgarian Development Bank AD (the parent company) signed a funds management contract with EIF for accession to the SIA investment program (SIA – Social Impact Accelerator) of EIF for investing in social venture funds, with the participation amounting to EUR 1 million over an engagement period of up to 5 years. The goal of the SIA program is to invest in small and medium-sized enterprises having considerable social impact. EIF is the manager of the program. The duration of the programme is 10 years.

As of 31 December 2018, twelve equity contributions were made under the initiative amounting to EUR 279 thousand equivalent to BGN 546 thousand (2017: BGN 180 thousand equivalent to BGN 353 thousand) (Note 20).

In 2015, the parent company (the Bank) launched a new program for indirect financing of micro, small and medium-sized businesses subject to a maximum of BGN 150,000 thousand. Under the program BDB will be able to assume part of the risk – up to 30 per cent of the amount of the individual sub-loans – on loans granted by partner banks to businesses. At 31 December 2018, the Bank signed agreements with five partner banks and

the so-formed portfolio of guarantees amounted to BGN 2,790 thousand (31 December 2017: five partner banks and portfolio of guarantees amounting to BGN 3,576 thousand).

In 2018, there were active agreements for portfolio guarantees with 11 banks, under the 2009-2013 guarantee scheme, to which the National Guarantee Fund (a subsidiary of BDB AD) is a party. The maximum term of these guarantees is up to 10 years. The total limit of funds provided to the banks for including loans in the portfolio amounts to BGN 146,500 thousand (2017: BGN 146,500 thousand). As of 31 December 2018, the approved amount of guarantees included in the portfolio of the partner banks amounted to BGN 6,378 thousand (2017: BGN 11,078 thousand), and the guaranteed debt amounted to BGN 2,661 thousand (2017: BGN 4,983 thousand).

In 2014, the National Guarantee Fund launched a new guarantee scheme. There are 13 active signed agreements with banks for portfolio guarantees under this scheme. Unlike the previous one, banks under the new scheme have the opportunity to include loans in the guaranteed by the NGF portfolio themselves, complying with the requirements of the scheme. The term for inclusion of loans into the guaranteed portfolio ends in September 2015 and the NGF guarantee is valid by September 2018. Only new loans to small and medium-sized enterprises with a maximum guarantee by the National Guarantee Fund of up to 50 per cent from the amount of the loan and no more than BGN 500 thousand are included in the guaranteed portfolio. There is a payment cap for each guarantee scheme under the 2014 guarantee scheme. The banks pay a guarantee fee based on the volume achieved, as the borrowers are exempt from fees on the guarantees provided by the NGF. The total limit granted to banks for the inclusion of loans in the portfolios amounts to BGN 192,000 thousand (2016: BGN 192,000 thousand).

The scheme was completed as at 31 December 2018. The approved amount of the guarantees included in the bank-partners. portfolios is zero (2017: BGN 49,047 thousand) and the amount of the guaranteed debt is zero (2017: BGN 39,009 thousand).

In 2015, a procedure for selecting partner banks of NGF under a new guarantee scheme was initiated. After performing the selecting procedures and conducting an analysis of the commercial banks, guarantee agreements were signed with 10 commercial banks for the total amount of BGN 326,000 thousand from the beginning of October 2015 to the beginning of January 2016.

In 2016, at request of two the banks having signed the agreement, the total guarantee limit was increased to BGN 379,000 thousand. Similar to the previous scheme, eligible for inclusion are only new loans for investment needs and working capital. According to the scheme, NGF guarantees up to 50 per cent of the loan amount, but not more than BGN 1 million at a related party level. The term for inclusion of loans into the guaranteed portfolio ends on 31 March 2017. A maximum limit of payments per guaranteed portfolio of up to 25 per cent is approved under the guarantee scheme, where in case of non-compliance with the terms and conditions of the scheme NGF has the right to exclude loans from the guaranteed portfolio. The banks pay a guarantee fee based on the volume achieved, while the borrowers are exempt from fees on the guarantees provided by the NGF. Since the start of the guarantee scheme, 2,024 SMEs were supported. The total limit granted to banks for the inclusion of loans in the portfolios amounts to BGN 379,000 thousand (2016: BGN 379,000 thousand). At 31 December 2018, the approved limit of the guarantees included in the partner banks. portfolios amounted to BGN 169,775 thousand (2017: BGN 209,598 thousand) and the guaranteed debt amounted to BGN 125,705 thousand (2017: BGN 169,038 thousand).

In the beginning of 2017, NGF commenced a procedure for extending the term of the guarantee scheme NGF 2015-2017 for a new term for inclusion. All banks had expressed an interest and new agreements were signed for the amount of BGN 328,000 thousand. As in the previous scheme, only new investment loans and loans for working capital are eligible for inclusion. According to the scheme, NGF guarantees up to 50% of the loan amount, but not more than BGN 1 million at the level of related parties. The term for inclusion of loans into the guaranteed portfolio ends in September 2018. There is a payment cap for each guaranteed portfolio of up to 25%, while NGF has the right to exclude credits from the guaranteed portfolio in case of non-compliance with the terms and conditions of the scheme. Banks pay a guarantee fee based on the volumes achieved and the borrowers are exempt from guarantee fees by the NGF.

By another annex, the total amount of funds provided to banks for inclusion of loans in the portfolio is BGN 416,131 thousand. At 31 December 2018, the approved limit of the guarantees included in the partner banks portfolios amounted to BGN 354,397 thousand (2017: BGN 126,493 thousand) and the guaranteed debt amounted to BGN 292,993 thousand (2017: BGN 123,907 thousand). 3,000 SMEs were supported.

In December 2016, an Agreement was signed between the European Investment Fund (EIF) and National Guarantee Fund EAD (NGF EAD), by virtue of which new EUR 40 million was ensured for financing of small and medium-sized enterprises in Bulgaria under the EC COSME Programme. The funds are ensured with the support of the European Fund for Strategic Investment (EFSI) underpinning the Investment Plan of Europe (the Juncker Plan).

EIF provides a guarantee line of EUR 20 million, through which NGF will support a financing of EUR 40 million to SMEs in Bulgaria experiencing difficulties in ensuring the required collateral. Five agreements for portfolio guarantees were concluded with five commercial banks: BACB AD, TBI Bank, MFI Jobs, First Investment Bank, and Eurobank Bulgaria AD. The maximum limit is BGN 43,338 thousand.

At 31 December 2018, guarantees of BGN 8,636 thousand (2017: BGN 3,574 thousand) were issued on 76 loans for the total amount of BGN 17,271 thousand (2017: BGN 7,147 thousand). The current guaranteed debt at 31 December 2018 amounts to BGN 8,636 thousand (2017: BGN 2,992 thousand). One hundred and eighteen SMEs were supported.

Based on a Financing Agreement signed with EAFA in 2011, NGF implements a guarantee scheme in the Fisheries sector. The guarantees issued by NGF pursuant to the Programme are risk-free as the claims are paid on account of the funds provided by OPDFS. Agreements with 16 commercial banks were signed under the NGF Programme. Thanks to the support of the scheme, projects amounting to BGN 46,000 thousand were implemented, of which BGN 33,000 thousand were for projects under Measure 2.1 (79 per cent of the measure.s budget); the projects supported under Measure 2.6 amounted to BGN 12,000 thousand (77 per cent of the measure.s budget). Projects under Measure 4.1 amounting to BGN 500 thousand were supported as well.

As of 31 December 2018, when applying the maximum amount of guarantee coverage of 80 per cent, NGF EAD had issued risk-free guarantees/counter guarantees for loans issued by partner banks for financing of approved projects under the Operational Programme “Fisheries Sector Development” 2007-2013 amounting to BGN 13,874 thousand with total amount of loans/bank guarantees – BGN 20,780 thousand (2017: guarantees BGN 13,874 thousand with total amount of loans/bank guarantees – BGN 20,780 thousand).

The carrying amount of the guaranteed debt as of 31 December 2018 was BGN 3,848 thousand (2017: BGN 4,959 thousand).

Based on a Financing Agreement signed with MAF in 2012, NGF performs guarantee activities in support of beneficiaries of OPRD 2007-2013. The guarantees issued by NGF under the Programme are risk-free for the Company as the claims are paid on account of the funds provided by OPRD. 544 beneficiaries of the Programme were supported for projects implementation under the scheme, whereas 84 per cent of the entities are classified as micro-, 14 per cent as small- and 3 per cent as medium-sized enterprises.

As of 31 December 2018, when applying the maximum amount of guarantee coverage of 80 per cent, NGF EAD had issued risk-free for the issuer guarantees/counter guarantees for loans issued by partner banks for financing of approved projects under the Operational Programme for Rural Development of Republic Bulgaria 2007-2013 amounting to BGN 185,606 thousand (2016: BGN 185,606 thousand) with total amount of loans of BGN 238,112 thousand (2017: BGN 238,112 thousand).

The total guarantee limit under this program at 31 December 2018 amounts to BGN 14,692 thousand (2017: BGN 24,254 thousand).

The guarantee scheme is a scheme implemented jointly with MAF, which is realized by funds amounting to BGN 50 million released under the guarantee scheme of OPRD 2007-2013 for financing projects approved under the Operational Programme for Rural Development of Republic Bulgaria 2014 – 2020. The guarantees issued by

NGF EAD under the Programme are risk-free for the Company as the claims are paid on account of the funds provided by OPRD.

At 31 December 2018, by applying the maximum guarantee cover amount of 50 per cent, NGF EAD issued risk-free guarantees and counter-guarantees for the Company on loans extended to partner banks for the purpose of financing projects approved under the Operational Programme for Rural Development of Republic Bulgaria 2014 – 2020 amounting to BGN 61,540 thousand (2017: BGN 92,028 thousand) with the total amount of loans being BGN 123,755 thousand (2017: BGN 45,750 thousand). The total guarantee limit of the Programme is BGN 50,000 thousand. At 31 December 2018, the loans guaranteed were 114 for the total amount of BGN 85,002 thousand. Ninety-six small- and medium-sized enterprises were supported. The book value of debt guarantees at 31 December 2018 is BGN 38,533 thousand (2017: BGN 34,483 thousand).

Nature of instruments and credit risk

These commitments of contingent nature bear an off-balance sheet credit risk because only fees are recognised in the financial statements until the commitments are fulfilled or expire. The amounts reflected in the above table as guarantees represent the maximum accounting loss that would have been recognised at the end of the reporting period if counterparties failed to perform in full their contractual obligations. Many of the contingent liabilities and commitments will expire without being advanced fully or partially. Therefore, the amounts do not represent expected future cash flows. Collateral for issuance of common bank guarantees exceeds 100 per cent and represents primarily restricted deposits at the Bank, mortgages of real estate and insurance policies issued in favour of the Bank. When conditions for enforcement of an issued guarantee occur, the Bank judges the possibilities for recourse to the counterparty and eventual realisation of the provided securities.

The guarantees of the parent company (the “Bank”), issued under the Micro-credits Guarantee Fund Project of MLSP, and the guarantees issued at own risk of NGF (subsidiary of BDB) are not secured. In case of activation of a component of a guarantee issued by the Group, the payment thereon is not assessed as ultimate loss because the partner-bank is obliged to undertake all necessary measures for realising the received collateral of the non-performing loan and to reimburse the respective amount to the Group.

The non-paid portion of the nominal value of EIF shares held by the Bank shall become due for payment after a special decision for this purpose taken by European Investment Fund’s General Meeting of Shareholders. By the issue date of this financial statement no such a decision has been taken.

36. CASH AND CASH EQUIVALENTS

In BGN.000	2018	2017
Cash in hand (Note 16)	335	244
Current account with the Central Bank (Note 16)	297,287	447,404
Receivables from banks with original maturity up to 3 months	320,139	74,652
	617,761	522,300

	1 January 2018	Cash inflows	Cash out- flows	Effect of changes in exchange rates	Accruals under the effective interest rate method*	Other	31 December 2018
Current borrowings from international institutions	869,822	156,254	(121,259)	(35)	-	-	904,782
Current liabilities on other borrowings	111,406	27	(1,102)	-	-	-	110,331
Total liabilities from financing activity	981,228	156,281	(122,361)	(35)	-	-	1,015,113

*The interest accruals of BGN 6,631 thousand were included in the operating cash flows of the Bank.

37. TRANSACTIONS WITH RELATED PARTIES AND COMPANIES UNDER JOINT CONTROL WITH THE STATE

Related parties:

The following table above shows the companies with which the Bank had transacted during the reporting period. All related party transactions were carried out at agreed prices.

Entity/person	Type of control
Ministry of Economy	Majority shareholder of the capital of the Bank representing the State
Ministry of Finance	Under joint control with the State
National Guarantee Fund EAD	Subsidiary
Micro Financing Institution EAD	Subsidiary
Capital Investments Fund EAD	Subsidiary
TC Maritsa EOOD	Subsidiary
Holding Bulgarian State Railways EAD	Company under joint control with the State
Bulgarian Institute for Standardization	Company under joint control with the State
South Stream Bulgaria AD	Company under joint control with the State
"I C J B" AD	Company under joint control with the State
Bulgarian Energy Holding EAD	Company under joint control with the State
Kinteks EAD	Company under joint control with the State
Energy Investment Company EAD	Company under joint control with the State
Water Supply and Sewerage EOOD Plovdiv	Company under joint control with the State
Water Supply and Sewerage EOOD Shumen	Company under joint control with the State
TPP Maritsa East 2 EAD	Company under joint control with the State
State Consolidation Company EAD	Company under joint control with the State
Eco Anthracite EAD	Company under joint control with the State
Saint Ekaterina University Multiprofile Hospital for Active Treatment	Company under joint control with the State
Montazhi EAD	Company under joint control with the State
Executive Agency Fisheries and Aquacultures	Company under joint control with the State
Ministry of Agriculture and Foods	Company under joint control with the State

Related party balances in the statement of financial position at the end of the reporting periods are as follows:

Assets			
<i>Entity/person</i>	<i>Type of balance</i>	2018	2017
Ministry of Finance	Securities at fair value through other comprehensive income	460,963	288,881
Company under joint control with the State	Loans and advances to customers	90,673	98,006
Company under joint control with the State	Securities at fair value through other comprehensive income	43,931	-
Liabilities			
<i>Entity/person</i>	<i>Type of balance</i>	2018	2017
Ministry of Finance	Other borrowings	17,306	17,492
Company under joint control with the State	Liabilities to customers on deposits and other borrowings	1,004,838	604,596

Related party transactions:

<i>Entity/person</i>	<i>Type of relationship</i>	2018	2017
Ministry of Finance	Fee and commission income	62	64
	Interest income	2,971	1,611
	Interest expenses	(124)	(128)
Company under joint control with the State	Interest income	4,883	7,830
	Fee and commission income	227	498
	Interest expenses	(257)	(977)
	Other operating income	34	210

Contingencies and commitments with related parties:

<i>Entity/person</i>	<i>Type</i>	2018	2017
Company under joint control with the State	Unutilised amount of loans approved	41,708	27,290
Company under joint control with the State	Bank guarantees issued	9,332	4,993
Company under joint control with the State	Letters of credit	-	-

Relations with key management personnel:

Balances with key management personnel		2018	2017
Payables to customers on deposits		320	371
Remuneration payable		120	68
Loans and advances to customers		142	405
Transactions with key management personnel		2018	2017
Remuneration and social security contributions		(2,290)	(2,075)
Interest expense		(1)	(1)
Interest income		4	4

38. EVENTS AFTER THE DATE OF THE FINANCIAL STATEMENTS

On 12 March 2019, Bulgarian Development Bank incorporated a subsidiary – BDB Leasing EAD with capital of BGN 2 million, fully paid-in, and with main object of activity: finance and operating lease of assets.

On 13 March 2019, Bulgarian Development Bank incorporated a subsidiary – BDB Factoring EAD with capital of BGN 2 million, fully paid-in, and with main object of activity: factoring.

Both companies were not operational as at the date of these financial statements.

In March 2019, Fitch Ratings Agency upgraded the outlook of the credit rating of Republic of Bulgaria from Stable to Positive. During the same month, the credit rating of Bulgarian Development Bank was upgraded from BBB, Stable Outlook to BBB, Positive Outlook.



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